AGENDA – March 26, 2003 Property Tax Committee Meeting
State Assessment Manual and *Unitary Valuation Methods* Book
Implementation of AB 81 and Property Tax Rule 905

Action 1 – Consent Item Agenda Item 1 Issue Paper 03-002	Adopt proposed amendments to the *State Assessment Manual* and the *Unitary Valuation Methods* book as agreed upon by staff and interested parties.
Action 2 – Status Report Agenda Item 2 Status Report	Staff's status report on the implementation of Assembly Bill 81 and Property Tax Rule 905, *Assessment of Electric Generation Facilities*

If you wish to have any consent items (Action 1) discussed fully at the committee meeting, you must contact a Board Member prior to March 21, 2003 to request removal of the item from the Consent Agenda.

Issue Paper Number **03-002**

BOARD OF EQUALIZATION
KEY AGENCY ISSUE

- ☐ Board Meeting
- ☐ Business Taxes Committee
- ☐ Customer Services and Administrative Efficiency Committee
- ☐ Legislative Committee
- ☒ Property Tax Committee
- ☐ Other

State Assessment Manual and *Unitary Valuation Methods* Book

I. Issue

Should the Board of Equalization authorize publication of the updates to the *State Assessment Manual* and the *Unitary Valuation Methods* book?

II. Staff Recommendation

Staff recommends that the attached updates to the *State Assessment Manual* and the *Unitary Valuation Methods* book be authorized for publication.

III. Other Alternative(s) Considered

None

IV. Background

Section 19 of article XIII of the California Constitution requires the Board to annually assess certain types of property. Such *state-assessed* property includes most property owned or used by public utility companies and railroads. The *State Assessment Manual* describes principles and procedures relevant to the assessment of state-assessed property. The *Unitary Valuation Methods* book describes the specific valuation models currently used by Board staff in the preparation of indicators of value. The *State Assessment Manual* was last revised in November 2000 and superseded an existing manual (Assessors' Handbook Section 541, *Assessment of Public Utilities and Railroads*) on the same subject, first published in May 1981. The *Unitary Valuation Methods* book was last revised in March 2000.

In 2002, staff initiated updates to both the *State Assessment Manual* and *Unitary Valuation Methods* book. The updates reflect statutory and regulatory changes, as well as recently adopted Board policy. Interested parties discussed the proposed changes at a meeting in Sacramento on January 24, 2003. At that meeting, the parties reached agreement as to the language in both publications.

V. Staff Recommendation

A. Description of the Staff Recommendation

Staff recommends that the attached updates to the *State Assessment Manual* and the *Unitary Valuation Methods* book be authorized for publication. The updates reflect current law and recently adopted Board policy as follows:

- Addition of section 100.9 which affects the allocation of assessed values and tax revenues derived from some electric generation facilities (Stats. 2002, Ch. 57).

- Addition of section 721.5 which requires the Board to assess most electric generating facilities with a capacity of 50 megawatts or more (Stats. 2002, Ch. 57).

- Amendment to section 749 which affects hearings on petitions for correction of allocated assessments (Stats. 2001, Ch. 744, SB 1182).

- Amendment to Property Tax Rule 21*, Taxable Possessory Interests – Valuation*; repeal of Property Tax Rule 23, *Written Agreements as to Term of Possessory Interests*; repeal of Rule 24, *Possessory Interest Rights to be Valued*; repeal of Rule 25, *Valuation of Post-De Luz Possessory Interests*; and repeal of Rule 26 *Valuation of Pre-De Luz Possessory Interests*.

- Adoption of Property Tax Rule 29, *Possessory Interests in Taxable Government-Owned Real Property*.

- Amendment to Property Tax Rule 905, *Assessment of Electric Generation Facilities*.

- Treatment of the ad valorem tax rate in the capitalization of income method employed to value possessory interests that is consistent with the Assessors' Handbook Section 510, *Assessment of Taxable Possessory Interests*.

- Treatment of deferred income taxes that is consistent with recently adopted Board policy.

- Delegation to county assessors of the duty to assess sites for wireless telecommunication towers.

B. Pros of the Staff Recommendation

Publication of the updated *State Assessment Manual* and the *Unitary Valuation Methods* book will ensure that Board guidance on the treatment of state-assessed property reflects the most recent statutory amendments, regulatory changes, judicial decisions, and Board policies.

C. Cons of the Staff Recommendation

None

D. Statutory or Regulatory Change

None

E. Administrative Impact

None

F. Fiscal Impact

1. Cost Impact

The estimated cost for printing and distributing copies of the updated *State Assessment Manual* and *Unitary Valuation Methods* book is $1,464.

2. Revenue Impact

None

G. Taxpayer/Customer Impact

None

H. Critical Time Frames

None

VI. Alternative 1

A. Description of the Alternative

Not applicable

Prepared by: Property and Special Taxes Department, Assessment Policy and Standards Division and Valuation Division
Legal Department, Property Taxes Section

Current as of: February 21, 2003

STATE ASSESSMENT MANUAL

DRAFT

~~NOVEMBER 2000~~MARCH 2003

FOREWORD

The *State Assessment Manual* describes the principles and procedures used by the Board in the assessment of state assessed property. It is designed to assist Board staff, state assessees and their representatives, county assessors and their staffs, and others with an interest in state assessment. This edition of the *State Assessment Manual* is an update of the manual that was rewritten in November 2000. ~~This~~ The November 2000 manual ~~revises~~ revised and ~~supersedes~~ superseded an existing manual (Assessors' Handbook Section 541, *Assessment of Public Utilities & Railroads*) on the same subject which was first published in May 1981.

Important topics covered include the following: state assessment jurisdiction, standard of value, the unit valuation concept, allocation of unitary value, and appeals of state assessments. Appendixes address several other aspects of state assessment, including the Private Railroad Car Tax, property transactions and jurisdictional changes, the Board's system of property classification codes, a calendar of important state assessment dates, and pertinent constitutional, statutory, regulatory, and judicial citations. The manual also contains a glossary and bibliography.

The manual was prepared within an open process that allowed input from industry representatives, county assessors, and others. Any issues regarding the manual's final language and contents that could not be resolved by consensus among interested parties were voted on and resolved by the Members of the Board of Equalization after hearing relevant testimony from interested parties and Board staff.

Under Government Code sections 15606 et seq., the State Board of Equalization is charged with the duty of administratively enforcing and interpreting the statutes governing the local assessment function. While regulations adopted by the State Board of Equalization are binding as law, Board-adopted manuals are advisory only. Nevertheless, courts have held that they may be properly considered as evidence in the adjudicatory process.[1] The citations and law references in this publication were current as of the writing of the manual.

~~Richard C. Johnson~~David J. Gau
Deputy Director
Property and Special Taxes Department
~~November 2000~~March 2003

[1] *Coca-Cola Co.* v. *State Board of Equalization* (1945) 25 Cal.2d 918; *Prudential Ins. Co.* v. *City and County of San Francisco* (1987) 191 Cal.App.3d 1142; *Hunt Wesson Foods, Inc.* v. *County of Alameda* (1974) 41 Cal.App.3d 163.

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CHAPTER 1: STATE ASSESSMENT JURISDICTION

HISTORICAL BACKGROUND

Under the California Constitution of 1849, the state's first, the property tax was the primary source of revenue for both state and local government. Local assessors were responsible for the assessment of all taxable property; the state had no assessment responsibilities. To support its operations, however, the state levied a separate state tax on the locally generated assessment rolls.

Under the Constitution of 1879, the Board of Equalization assumed responsibility for the centralized assessment of the roadway, roadbed, rails, rolling stock, and franchises of intercounty railroads, marking the beginning of state assessment in California. The Board's assessments were apportioned to the local assessment rolls; all other property remained subject to assessment by the local assessor of the county in which the property was situated. There was no change in the way taxes were levied by the state and local jurisdictions—both continued to levy a tax against the local assessment rolls.[2]

Under a constitutional amendment of 1910, implemented through the Comprehensive Tax Act of 1911, the state, and hence the Board, took a leave of absence from the assessment function for roughly a quarter of a century. The primary feature of this legislation was to separate the sources of state and local tax revenues. State government was supported by a new set of taxes levied exclusively for state purposes in lieu of property taxes. The in-lieu taxes reached a number of industries and were levied as follows:

1. On gross receipts from operations of railroad companies, gas and electric companies, telephone and telegraph companies, car companies and express companies, in lieu of all other taxes and licenses on the operating property of such companies.

2. On gross premiums of insurance companies in lieu of all other taxes and licenses, except local taxes on real property.

3. On capital stock of banks in lieu of all other taxes and licenses on such stock and on the banks except local taxes on real property.

4. On all franchises, general, corporate and special, except franchises held by public utilities, insurance companies, or banks otherwise taxed for state purposes.

While the Board was charged with assessing the foregoing companies for the in-lieu tax levies, all other property remained locally assessed and subject to ad valorem property taxation for the support of local government.

[2] Under the Constitution of 1879, only railroad property was subject to state assessment, and only enumerated types of railroad property.

In 1933, a state fiscal crisis led to a constitutional amendment producing significant tax reform. The resulting Riley-Stewart Plan for tax relief, perhaps best known for introducing the sales and use tax to California, abandoned the in-lieu gross receipts tax and once again made the property of "public utilities" subject to ad valorem taxation. The plan retained the feature of central assessment by the Board introduced in the Constitution of 1879, and extended the Board's assessment jurisdiction to a broader class of "public utilities" and to all of the taxable property of certain types of enterprises. As previously, state assessments were allocated to the local assessment rolls for the purpose of local property taxation, but now no state tax was levied on the local rolls. The current jurisdiction of state assessment, described in greater detail below, essentially derives from the constitutional amendment of 1933, as does the state's present tax structure, in which non-property tax sources support state government (primarily the sales and use tax and the income tax) and property taxes support local jurisdictions.

CONSTITUTIONAL PROVISIONS

Section 19 of article XIII of the California Constitution requires the Board to annually assess certain described types of property. The first paragraph of section 19 divides this property into two categories:

> The Board shall annually assess (1) pipelines, flumes, canals, ditches, and aqueducts lying within 2 or more counties and (2) property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the State, and companies transmitting or selling gas or electricity. This property shall be subject to taxation to the same extent and in the same manner as other property.

The first category of property consists of specific types of improvements, that is, pipelines, flumes, canals, ditches, and aqueducts lying within two or more counties. The important qualification with regard to this category is that the properties are located "within two or more counties," without regard to the nature of the property owner. For example, if an oil company owns a pipeline lying within two or more counties, the Board is required to assess the pipeline but not other property owned by the oil company.

The second category of property consists of all taxable property, excluding franchises, owned or used by regulated railway, telegraph, or telephone companies; car companies operating on railways in the state; and companies transmitting or selling gas or electricity. Rather than being based on the type of property to be assessed, this category includes *all* of the property that is owned or used by specified types of companies. Under this category, all of the property owned or used by a specified company is subject to the Board's assessment. For example, Southern Pacific Railroad was at one time the largest private property owner in the state. For historical reasons, it owned large tracts of land in addition to the property owned or used for railroad purposes. Under section 19, the Board is required to assess all of its property, including the tracts of land not actually used for railroad purposes.

The provisions of the Revenue and Taxation Code implementing section 19 of article XIII are found in sections 721 and following.[3] Section 721 states that the Board shall annually value and assess all of the taxable property within the state that is to be assessed by it pursuant to section 19 of the California Constitution and any legislative authorization thereunder. Section 721, however, does not provide any definition or detail regarding the type of property to be assessed beyond that listed in section 19 of article XIII.[4]

Several historical reasons led to central assessment by the Board most of which derived from perceived problems associated with the assessment of railroad property during the 1870's, shortly after California's statehood. These issues mirrored those in several eastern and Midwestern states that arose slightly earlier.

First, early railroads were the first entities to operate across county, and often state, boundaries. The "continuous property" of railroads (e.g., roadway, roadbed, and rails) was assessed markedly differently among counties. This created a significant problem related to intercounty uniformity and equalization of assessment, a mandate of the state's first Constitution. Centralized assessment was also considered the most efficient assessment solution for "migratory properties," such as private railroad cars, because of the difficulty of determining the location, or situs, of such properties on the lien date.

A second consideration involved doubts regarding the ability of local assessors to render equitable assessments given the political power of the early railroads. In this context, state assessment represented a countervailing power.

Finally, there was a concern that the "true value" of railroad property as part of an operating unit, or going concern, was not being reflected in the separate assessments of the local assessors.

SOME JURISDICTIONAL PRINCIPLES

Over the years, there have been numerous interpretations of the language in section 19 of article XIII, by the Board itself and others, relating to the Board's assessment jurisdiction. This section discusses some of the principles that have emerged and how they have been applied.

First, as a quasi-judicial, constitutional body, the Board has the right to determine its own jurisdiction in the first instance. In essence, this means that the Board has the right to pass on its own jurisdiction first, and that this determination will stand unless overruled by a higher legal

[3] All references to "section 19" refer to article XIII of the California Constitution. All other "section" references refer to a section of the Revenue and Taxation Code, unless otherwise designated.

[4] ~~Some assessment statistics put state assessment in perspective. For 1999-2000, the value of all property assessed in California – by the 58 county assessors and the Board – was about $2,244 billion. The value of property assessed by the Board was about $69 billion. Thus, state assessments constitute about 3 percent of all property assessments in the state.~~

~~There are roughly 690 state assessees. State assessments, however, are highly concentrated. The 8 largest state assessees, for example, received property assessments of about $57 billion, roughly 85% of the $69 billion total of state assessments. (Board data.)~~

authority. This power stems from other powers conferred on the Board in sections 11, 17, 18, and 19 of article XIII of the State Constitution that are quasi-judicial in nature and on the Board's status as an agency of constitutional origin.

Second, the Board's assessment jurisdiction over property owned by various types of common carrier (i.e., transportation) and public utility companies extends both to those that are "regulated" and those that are "unregulated." For example, section 19 of article XIII grants the Board jurisdiction to assess "property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the state, and companies transmitting or selling gas or electricity." In this passage, the word "regulated" does not modify "car companies" or "companies transmitting gas or electricity." Thus, the Board's jurisdiction does not extend to unregulated railway, telegraph, or telephone companies, but may extend to car companies and companies transmitting or selling gas or electricity whether or not such companies are regulated.[5]

The majority of companies whose property the Board has historically assessed have been regulated in the sense that they hold certificates of public convenience and necessity (CPCN) from the California Public Utilities Commission (CPUC), or in the sense that many communications companies are regulated by the Common Carrier Bureau of the Federal Communications Commission (FCC).

Until recent years, many companies subject to state assessment were also rate-regulated, meaning that in exchange for certain monopoly rights over a designated franchise or service area, the companies were limited in the rates they could charge. Other companies were, and some still are, rate-base/rate-of-return regulated, meaning that the rates, or income, that regulators allow such companies to earn are designed to cover costs, including taxes and depreciation, and also provide a "fair" rate of return on investment, often as measured by a fair rate of return on rate base. Rate base, with some modifications, is essentially the book, or accounting, value of the company's assets used in providing service. With the deregulation of several industries in recent years, however, the majority of state assessees are no longer subject to rate regulation or rate-base/rate-of-return regulation.

Third, while the Board historically has assumed jurisdiction of all investor-owned "public utilities," some state assessees are not public utilities in the common meaning of that term. A definition of "public utilities" from section 3, article XII, of the California Constitution provides, in part:

> Private corporations and persons that own, operate, control, or manage a line, plant, or system for … the production, generation, transmission, or furnishing of heat, light, ... power, … directly or indirectly to or for the public, … are public utilities subject to control by the Legislature….

[5] By interpretation, see Proposed Revision of California Constitution, article XIII, Appendix to Senate Daily Journal, May 14, 1974, p.27; by application, see Rule 905 of Title 18, Public Revenues, California Code of Regulations, *Assessment of Electric Generation Facilities.*

Some of the types of state assessees enumerated in section 19 of article XIII are within the above definition of investor-owned public utilities and some are not. For example, many companies that own pipelines, canals, or aqueducts are not public utilities by this definition. Consequently, the Board does not rely on a definition of "public utilities" as the touchstone of its jurisdiction. Rather, the Board has consistently assessed only those types of property and the property of those types of companies enumerated under section 19 of article XIII, whether or not the companies are "regulated" or meet the definition of a "public utility." The Board's determination of jurisdiction does not rest on the outward appearances of a property or company, but rather on whether the Board concludes that section 19 article XIII provides the Board with jurisdiction to assess. A recent example of the Board determining both the extent and limits of its jurisdiction under section 19 of article XIII occurred as a result of the restructuring of the electric industry, which is discussed in further detail below under that specific area of the Board's jurisdiction.

SPECIFIC AREAS OF BOARD JURISDICTION

RAILROADS AND PRIVATE RAILROAD CARS

The property of "regulated railways" is specifically enumerated in section 19 of article XIII as subject to state assessment. All railways are regulated in that they are subject to safety and common carrier regulation by the United States Department of Transportation. The Board holds assessment jurisdiction over all railways, including so-called "shortline railroads"—those that own track and are located within only one county.[6]

The property of "car companies operating on railways in the state" is also specifically enumerated in section 19 of article XIII. The Private Railroad Car Tax, at sections 11201 and following, prescribes a specific method for the assessment of this type of property. As unambiguously defined in section 11203, a "private railroad car:"

> … includes any railroad rolling stock intended for the transportation of any persons, commodity, or material, operated on the railroads of this state, which car is owned by a person other than a railroad or the National Railroad Passenger Corporation….

In addition to assessing private railroad cars, the Board also levies and collects the corresponding tax, which is deposited in the state's General Fund.[7]

[6] In a transportation-industry context, a "common carrier" can be defined very generally as an entity engaged in transporting persons, goods, or messages for the public over a regular route, according to specified schedule, and for an approved charge or fee, all of which are usually subject to government regulation. Common carriers are deemed to be "affected with the public interest" and are regulated by the U.S. Department of Transportation.

[7] Appendix A describes the Private Railroad Car Tax in more detail.

INTERCOUNTY PIPELINES

As previously discussed, intercounty pipelines are subject to Board assessment because of the type of property they are and because they are located within two or more counties, not because of the nature of their ownership.

In *Southern Pacific Pipe Lines, Inc.* v. *State Board of Equalization* (1993), the court held that the Board could not assess three pipeline facilities because the facilities were not essential and necessary to the operation of intercounty pipelines.[8] The court held that the term "pipelines" in section 19 referred to the pipelines only, not to the underlying land or rights-of-way or to adjacent lands and improvements. This holding was later codified in sections 401.10 and following. Each county assessor, therefore, has jurisdiction to locally assess *all lands and rights-of-way* in his or her county over or through which pipelines cross. The decision in *Southern Pacific Pipe Lines, Inc.*, however, did not address the other types of property enumerated in paragraph (1) of section 19 of article XIII—that is, flumes, canals, ditches and aqueducts lying within two or more counties—in this context.

TELEPHONE COMPANIES

Section 19 of article XIII mandates Board assessment jurisdiction concerning "property, except franchises, owned or used by regulated … telephone companies.…" The term "regulated telephone company," however, is not defined by the California Constitution, statutory provisions, or the courts in the context of assessment jurisdiction.

As with other state assessees, the Board has interpreted section 19 of article XIII as requiring Board jurisdiction of only telephone companies regulated as public utilities by the California Public Utilities Commission (CPUC) or by a comparable federal commission or board—for example, the Common Carrier Bureau of the Federal Communications Commission (FCC). The Board has treated as "public utilities" telephone companies that have been granted a certificate of public convenience and necessity from the CPUC or that have been classified as communications common carriers by the Common Carrier Bureau under federal law.[9] The Board's practice has been to assess the property of only those telephone companies that are regulated public utilities under either state or federal law.

Long distance resellers and alternative operator services doing business in this state are generally regulated by the CPUC; if they own or lease property in California, the property is subject to Board assessment (e.g., some resellers have their own switching systems in California). If they do

[8] 14 Cal.App.4th 42.
[9] See 29 Ops.Cal.Atty.Gen. 77; and 47 U.S.C.A. 201 and following.

not own or lease facilities in California, however, they are not required to file a property statement and the Board has no assessment jurisdiction over them.[10]

Some telephone companies and resellers now use satellite transmission that replaces existing wire, fiber, and cellular systems. The FCC is the only regulatory agency that issues permits (i.e., licenses) for the operation of such companies; the CPUC has no regulatory authority. To the extent that the companies own property in California, they are under the Board's assessment jurisdiction, consistent with the Board's position that telephone companies are "regulated" if their permits or operating rights are prescribed by either state or federal law.

Also, some companies formerly operated for other purposes may begin telephone service and thereby become subject to Board jurisdiction. For example, if a cable television company decides to offer telephone services, and obtains authorization under state or federal law for this purpose, all of the company's property then would be subject to the Board's assessment jurisdiction—the company would meet the definition of a "regulated" telephone company.[11]

Occasionally, in such a scenario, the telephone and the cable television operations might be conducted by separate corporations or other legal entities. When companies subject to the Board's assessment jurisdiction form new subsidiary or affiliate companies, wholly owned either directly or indirectly by the parent company, the "separate legal entity" concept controls whether the Board's assessment jurisdiction extends to the newly created entity. For example, if the newly created entity is the subsidiary of a telephone company, but never obtains either a certificate of public convenience and necessity from the CPUC, or becomes subject to regulation by the FCC as a communications common carrier, then it will not come under the Board's assessment jurisdiction. However, if it operates under the parent company's certificate or common carrier status (or if it acquires either one on its own), it is considered a "regulated" telephone company and will become subject to the Board's jurisdiction.

[10] Long distance resellers and alternative operator companies obtain a CPCN to offer telecommunication services over the facilities of the local exchange carrier. The certificate grants resellers and alternative operator companies the right to do business with a local exchange carrier at a discounted rate, which frequently enables them to offer less expensive long-distance service. The CPUC grants certificates to such companies because the public interest is served by promoting effective competition among telecommunications service suppliers. Whether or not resellers actually lease or purchase the use of a switch or any of the facilities of the local exchange carrier is a matter of agreement between the companies involved in each case.

[11] An emerging issue in this regard is the regulatory classification of high speed Internet access services. In a Notice of Inquiry involving cable modem service, the FCC noted, "Service providers are deploying a variety of networks that rely on different network architectures and transmission paths, including copper wire, cable, terrestrial wireless radio spectrum, satellite radio spectrum, or a combination of these and other media, to provide high-speed services." (Gen Docket No. 00-185, "*Inquiry Concerning High-Speed Access to the Internet Over Cable and Other Facilities*," par. 7). As regulatory issues concerning these services are resolved by the FCC, there may be jurisdictional concerns for the Board to consider, to the extent that the FCC or the CPUC regulate Internet access services as telephone services. For continuing developments on this subject, see www.fcc.gov.

INTEREXCHANGE AND COMMERCIAL MOBILE RADIO SERVICE

Similarly, interexchange and commercial mobile radio service companies are subject to the Board's assessment jurisdiction only if they can be classified as "regulated telephone companies" pursuant to section 19 of article XIII.[12]

The FCC allocates radio frequencies, or channels, to both public and private radio carriers. Prior to 1995 legislation and the FCC's resulting deregulation in 1996, the CPUC classified all public radio carriers (i.e., those authorized to provide service to the general public) as regulated radio telephone utilities, and required a CPCN for their operations. In 1995, subdivision (b)(2) of section 234 of the Public Utilities Code was amended to exclude "any one-way paging service facilities that are licensed by the Federal Communications Commission" from CPUC regulation.[13] Two-way paging companies were specifically excepted from the amending legislation and the amended statute. Based on this change in state law, the Board determined that for the 1996 lien date and thereafter one-way paging companies and narrow-band personal communications services that are not otherwise subject to Board jurisdiction will be assessed by county assessors because, statutorily, these companies are not "telephone companies."

Similarly, the Board has concluded that property used in the satellite transmission of voice communications should be excluded from its assessment jurisdiction when the system is used for television broadcast or other one-way transmission. In the Board's view, such systems do not meet the constitutional definition of a regulated telephone company.

GAS AND ELECTRIC COMPANIES

Until 1996, property owned by all gas and electric companies was subject to Board assessment. The only significant exception was electric cogeneration plants, which had historically been locally assessed. In 1996, however, legislation restructured the electric industry in California, excepting many companies that were and/or would be generating and selling electricity from rate regulation by the CPUC.[14]

One of the main objectives of restructuring, or deregulation, was to achieve a more competitive market for electric power by allowing new market entrants to purchase or build electric generation plants and sell electricity to the public. This was accomplished, in part, by requiring existing regulated companies with power generation and distribution facilities to sell power to a Power Exchange, an entity that acts as a market facilitator for the purchase and sale of electric power and that was created by the legislation.

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[12] A "commercial mobile service" is "any mobile service ... that is provided for profit and makes interconnected communication service available (a) to the public or (a) to such classes of eligible users as to be effectively available to a substantial portion of the public, as specified by regulation by the Commission." A "private mobile service" is "any mobile service that is the functional equivalent of a commercial mobile service, as specified by regulation by the Commission." An "interconnected service" is a "service that is interconnected with the public switched network (as such terms are defined by regulation by the Commission) or service for which a request for interconnection is pending." (47 U.S.C.A. §332, subdivision (d).)

[13] Chapter 357, Statutes of 1995 (Assembly Bill 202)

[14] Chapter 854, Statutes of 1996 (Assembly Bill 1890)

To address the jurisdictional implications of electric industry restructuring, legislation enacted section 721.5 and the Board adopted Rule 905.[15] Section 721.5 and Rule 905 limits the Board's assessment jurisdiction in regard to electric generation facilities. Rule 905 ~~It~~ states:

> (a) Commencing with the assessment for the lien date for the 2003 assessment year, an ~~An~~ electric generation facility shall be state assessed property for purposes of article XIII, section 19 of the California Constitution if: ~~(1) the facility was constructed pursuant to a certificate of public convenience and necessity issued by the California Public Utilities Commission to the company that presently owns the facility; or (2) the company owning the facility is a state assessee for reasons other than its ownership of the generation facility or its ownership of pipelines, flumes, canals, or ditches, or aqueducts lying within two or more counties.~~ (1) the facility has a generating capacity of 50 megawatts or more; and (2) is owned or used by a company which is an electrical corporation as defined in subdivisions (a) and (b) of section 218 of the Public Utilities Code; or, the facility is owned or used by a company which is a state assessee for reasons other than its ownership of the electric generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.
>
> (b) "Electric generation facility" does not include a qualifying small power production facility or a qualifying cogeneration facility within the meaning of Sections 201 and 210 of Title II of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. §§796(17), (18) and 824a-3) and the regulations adopted for those sections under that act by the Federal Energy Regulatory Commission (18 C.F.R. 292.101-292.602).
>
> (c) For purposes of this section, "company" means:
>
> (1) A person as defined in Revenue and Taxation Code section 19;
>
> (2) A separate division or other functional unit of a business enterprise which is created and maintained to operate any electric generation facility, where the business enterprise is engaged in a primary business other than generating, transmitting, distributing or selling electricity to the public.
>
> (d) If an electric generation facility is operated by a separate division or other functional unit of a business enterprise, as described in this rule, the business enterprise must maintain accounting and other records sufficient to distinguish the costs and revenues of the separate division or unit from other divisions and units of the business enterprise.
>
> (e) As adopted on September 1, 1999 and effective November 27, 1999, this rule is applicable to define electric generation facilities subject to state assessment to

[15] All references to "rule" refer to a rule in Title 18, Public Revenues, California Code of Regulations.

and including December 30, 2002. As amended on November 28, 2001, and filed with the Secretary of State on May 14, 2002, this rule is applicable to define electric generation facilities subject to state assessment as of December 31, 2002 and thereafter.

~~Therefore, there has been a shift from state to local assessment of some electric generation facilities. These facilities were assessed by the Board in 1998 but were subsequently sold to independent power companies that do not come under Board assessment jurisdiction under the provisions of rule 905. About seven investor-owned public utilities (with both power generation and distribution facilities) remain subject to rate regulation and are still considered "public utilities" by the CPUC. Under rule 905, the property of these companies continues to be assessed by the Board.~~

Section 721.5 was enacted and Rule 905 was amended to provide that electric generation facilities shall be state assessed property if the facility has a generating capacity of 50 megawatts or more and the facility is owned or used by a company that is an electrical corporation as defined in section 218 of the Public Utilities Code, or the facility is owned or used by a company which is a state assessee for reasons other than its ownership of an electric generation facility or its ownership of pipeline, flumes, canals, ditches, or aqueducts lying within two or more counties.

Further, section 721.5 and Rule 905 specifically exclude from state assessment electric generation facilities that are qualifying small power production facilities or qualifying cogeneration facilities within the meaning of sections 201 and 210 of Title II of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. sections 796 (17), (18) and 824a-3). The amended rule defines "company" to include separate divisions or other functional units of a business enterprise which have been created and maintained to operate any electric generation facility and to require the maintenance of certain accounting records.

Some companies engaged in the transmission of gas are not regulated by the CPUC because they are interstate natural gas pipeline companies that sell and deliver natural gas in interstate commerce. These companies are, nevertheless, considered public utilities in that they deliver their product to various locations in California under the exclusive authority and rate regulation of the Federal Energy Regulatory Commission. The Board's assessment jurisdiction also extends to this category of gas company.

BOARD JURISDICTION INCLUDES UNITARY AND NONUNITARY PROPERTY

An important statutory distinction made in regard to property types assessed by the Board is that found in sections 723 and 723.1, the distinction between unitary and nonunitary property. Unitary property is property used in the primary function of an assessee; nonunitary property is property owned by the assessee but not used in the assessee's primary function. The distinction between unitary and nonunitary is discussed in more detail in a later chapter. For the purpose here, suffice it to say that section 19 of article XIII requires the Board to assess property that is "owned or used" by a state assessee. This means that both the unitary and nonunitary property of a state assessee is subject to Board assessment. For example, a campground owned by a gas

company, even though it is not used in the company's utility operations, would still be assessed by the Board as the assessee's nonunitary property.

STATE ASSESSMENT PROCESS

To provide an overview of the general process of state assessment, several major steps in the process are described in roughly chronological order below. These steps also point to the subject matter discussed in subsequent chapters.[16]

1. The assessee files a property statement as required by section 826. Property statements must be filed no later than March 1 of each year; but the Board *may* grant limited extensions for specified parts of the property statement under section 830.1.

   The Board prescribes several variations of the property statement, depending on the type of property reported or the industry of the assessee. In general, however, the variations share the following common elements: (1) a declaration of costs and other related property information; (2) a tangible property list; (3) summary control accounts; (4) a statement of land changes and land identification maps; (5) schedules of leased equipment; and (6) other requested information.

2. The Valuation Division, a unit of the Board's Property and Special Taxes Department, develops unitary valuation indicators and makes recommendations to the Board regarding the value of the assessee's unitary property. State assessees are afforded an opportunity to discuss the value of their unitary property at a public Board meeting held in May.

3. The Board determines the value of the assessee's unitary and nonunitary property. Unitary value determinations are made and publicly announced no later than May 31. Nonunitary value determinations are made and announced no later than the last day of June. (Chapter 4 discusses value indicators.)

4. If a state assessee operates in more than one state, a portion of the value of the assessee's unitary property is allocated by the Board to California (interstate allocation). The portion of the value of the assessee's unitary property allocated to California—or, the total value of the assessee's unitary property if the assessee's operations are only in California—is allocated by the Board among the counties in which the property is located (intrastate allocation). (Chapter 5 discusses value allocation.)

5. For unitary and nonunitary values determined by the Board, the state assessee may file a petition for reassessment. (Chapter 6 discusses the appeals process for state assessments.)

[16] Appendix D is a calendar of important dates in the annual state assessment cycle.

CHAPTER 2: STANDARD OF VALUE

In any appraisal, there are two primary conceptual issues that must first be addressed: (1) the standard of value, or value concept, that is being sought and (2) the unit of property that is being valued. This chapter discusses the first of these conceptual issues; the following chapter discusses the second.

MARKET VALUE STANDARD

Section 1 of article XIII of the California Constitution states:

> Unless otherwise provided by this Constitution or the laws of the United States.
>
> (a) All property is taxable and shall be assessed at the same percentage of fair market value. When a value standard other than fair market value is prescribed by this Constitution or by statute authorized by this Constitution, the same percentage shall be applied to determine the assessed value. The value to which the percentage is applied, whether it be the fair market value or not, shall be known for property tax purposes as the full value.
>
> (b) All property so assessed shall be taxed in proportion to its full value.

Thus, the standard of value, or value concept, by which all state assessed property is assessed is "fair market value."[17] With the exception of restricted value property, whose value is statutorily prescribed at a standard other than market value as recognized in the second sentence of subdivision (a) above, this is the same value standard applied to locally assessed property.[18]

Section 110 describes the concept of market value. As provided in subdivision (a):

> Except as is otherwise provided in Section 110.1, "full cash value" or "fair market value" means the amount of cash or its equivalent that property would bring if exposed for sale in the open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other, and both the buyer and the seller have knowledge of all the uses and purposes to which the property is adapted and for which it is capable of being used, and of the enforceable restrictions upon those uses and purposes.

[17] Prior to 1981, property was assessed at a percentage of fair market value; this percentage was called the assessment ratio. Since 1981, property has been assessed at 100 percent of fair market value, an assessment ratio of 1.0.

[18] Several terms are used synonymously with "fair market value" in property tax statutes and regulations. These include "full cash value," "cash value," "actual value," and "market value."

Salient elements of the above definition include the following:

- Market value is measured in the "amount of cash or its equivalent." This means that the sale price of the subject property or sales prices of comparable properties used as evidence of market value should be stated in terms of cash.

- The property is "exposed for sale in the open market." This means that potential buyers are aware that the property is for sale and have sufficient time and opportunity to present their offers.

- Neither buyer nor seller "could take advantage of the exigencies of the other." This renders buyer and seller as hypothetical persons dealing with each other at arm's length—that is, neither is influenced by special motivations or particular circumstances.

- Buyer and seller "have knowledge of all the uses and purposes to which the property is adapted." The value of property depends on its use. This passage means that buyer and seller are aware of the highest and best use of the property, which is the lawful use that maximizes the property's value, and consider the value of the property in light of such use. In other words, buyer and seller are prudent, rational economic beings.

Subdivision (b) of section 110 establishes a rebuttable presumption that "full cash value" or "fair market value," as defined in subdivision (a), is the actual purchase price if the terms were negotiated under specified conditions reflecting an "open market transaction." Under subdivision (c), this rebuttable presumption does not apply when a taxpayer has failed to provide certain information about the conditions of the transaction.

Subdivisions (d), (e), and (f) of section 110 address the treatment of intangible assets and rights. Subdivision (d) provides that: (1) the value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property; (2) if the principle of unit valuation is used to value properties that are operated as a unit, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit; and (3) the exclusive nature of a concession, franchise, or similar agreement is an intangible asset that shall not enhance the value of taxable property, including real property.[19]

However, in applying the above principles, the Legislature stated at the beginning of subdivision (d) that its provisions are expressly subject to the language in subdivision (e). Subdivision (e) states: "Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the property to beneficial or productive use."

Finally, subdivision (f) of section 110 provides that for the purpose of determining "full cash value" or "fair market value," any intangible attributes of real property shall be reflected in the

[19] For additional discussion of the market value concept, see Assessors' Handbook Section 501, *Basic Appraisal*, and Assessors' Handbook Section 502, *Advanced Appraisal*.

value of the real property, and that these attributes include zoning, location, and other such attributes that relate directly to the real property involved.

In any given market, the variables that determine supply and demand, and hence market value, are subject to change—sometimes rapid change. An important consideration regarding market value, therefore, is that it is something that exists as of a given point in time. It is, therefore, necessary to specify a date of valuation in any consideration of market value. Accordingly, section 722 specifies that state assessed property is valued as of 12:01 a.m. on January 1, the lien date for property tax purposes.

STATE ASSESSED PROPERTY AND ARTICLE XIII A OF THE CALIFORNIA CONSTITUTION[20]

In June 1978 California voters passed an initiative constitutional amendment that significantly restructured California's property tax system. Proposition 13, which added article XIII A to the California Constitution, contained four primary elements: (1) a limit on the ad valorem property tax rate to 1 percent of the assessed value (except in the case of pre-existing bonded indebtedness or subsequent bonded indebtedness approved by a two-thirds vote); (2) a rollback of assessed values to their 1975-76 levels; (3) a limit on the annual growth in assessed value to a maximum of 2 percent per year, in the absence of a change in ownership or new construction; and (4) reassessment at current market value only upon a change in ownership or new construction.

In *ITT World Communications, Inc.* v. *City and County of San Francisco*, the California Supreme Court ruled that article XIII A's assessment rollback, its 2 percent limit on annual assessment growth, and its limit on current market value assessment only upon a change in ownership or new construction did not apply to state assessed property, only to locally assessed property.[21] As a result, taxable property in California is now generally split into two major categories: locally assessed property subject to the assessment limitations of article XIII A and state assessed property not subject to the assessment limitations of article XIII A.

In reaching its decision, the court presented the following major arguments. First, it held that article XIII A, by its own terms, was limited to real property taxation, but that the "unit taxation" of state assessed property was not real property assessment in substance or form. Second, it held that because article XIII A used the phrase "county assessor's valuation," again, by its own terms, the article applied only to locally assessed property. Third, and finally, the court held that the phrase "subject to taxation to the same extent and in the same manner as other property" from section 1 of article XIII of the California Constitution did not impose a requirement of valuation on the same basis between public utility and other property, but simply specified that state and local assessments must be levied at the same tax rate.

[20] Although not strictly about the "market value standard," this section relating to state assessed property and article XIII A and the next section relating to the Railroad Revitalization and Regulatory Reform Act are included here because both relate to the method of assessment for state assessed property.

[21] *ITT World Communications, Inc.* v. *City and County of San Francisco* (1985) 37 Cal.3d 859.

RAILROAD REVITALIZATION AND REGULATORY REFORM ACT

Congress enacted the Federal Railroad Revitalization and Regulation Reform Act (4-R Act) in 1976. The general purpose of the Act, as stated in section 801 of Title 45 of the United States Code, is

> [t]o provide the means to rehabilitate and maintain the physical facilities, improve the operations and structure, and restore the financial stability of the railway system of the United States.…

Another objective of the Act is to prohibit states from adopting tax structures that discriminate against railroads. Specifically, section 11501 of Title 49 of the United States Code prohibits the assessment of railroad property at a higher ratio to current market value than the analogous ratio for commercial and industrial property generally.[22]

The 4-R Act itself does not distinguish between the real and personal property of railroads. In *Trailer Train Co.* v. *State Board of Equalization*, however, the court concluded that personal property, specifically private railroad cars, is subject to the same assessment standards and limitations as real property.[23] Thus, the same "effective tax rate" that is applied to commercial and industrial property generally must be applied not only to all railroad property but also to private railroad cars. In this context, effective tax rate means the assessment ratio multiplied by the actual property tax rate.

To comply with the 4-R Act, the Board must ensure that all railroad property and private railroad cars are assessed at the same percentage of (or ratio to) current market value as other commercial and industrial property. For example, if for commercial and industrial property the ratio of assessed value to current market value is 83 percent, then the current market values of all railroad property and private railroad cars must be multiplied by 83 percent to arrive at their taxable values.

Board staff calculates the statewide ratio of assessed value to current market value for commercial and industrial property in an annual assessment ratio study. In essence, the sum of the assessed values of locally assessed land, non-fixture~~s~~ improvements, fixtures, and personalty and the assessed value of all state assessed property is divided by the corresponding sum of their respective estimated current market values.

The resulting percentage is generally less than 100 percent because locally assessed real property is assessed under the provisions of article XIII A of the California Constitution, which prescribes a base year assessment method that often results in a taxable value lower than current market value.

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[22] As defined in *Trailer Train Company* v. *State Board of Equalization* (1983) 697 F.2d 860, commercial and industrial property "means property, other than transportation property and land used primarily for agricultural purposes or timber growing, devoted to a commercial or industrial use and subject to a property tax levy."

[23] *Trailer Train Co.* v. *State Board of Equalization* (1983) 697 F.2d 860

CHAPTER 3: VALUATION USING THE UNIT CONCEPT

APPRAISAL UNIT AND THE PRINCIPLE OF UNIT VALUATION

The second major conceptual problem that must be resolved in any appraisal is a determination of the unit of property to be valued—that is, the property for which a market value estimate is sought. This problem is not limited to the central assessment of public utility property; it appears in every appraisal as the familiar question of the proper appraisal unit. When an appraiser decides on the proper unit of property to be valued, he or she has determined to not add up the values of any smaller units to arrive at the value of the unit.

In the context of the central assessment of public utility property, the problem of appraisal unit has been analyzed using a concept called the "principle of unit valuation." Other terms used synonymously include "unit valuation," "unit method," "unit concept," or "unit approach."

The principle of unit valuation holds, in essence, that a collection of tangible assets functioning as an operating unit should be valued as a whole, without reference to the separate values of the assets constituting the operating unit. A unit valuation is contrasted with a "summation valuation," in which the component parts of an operating unit are valued separately and summed to estimate the value of the whole. Under the principle of unit valuation, the Board may recognize the entire operating unit as the proper appraisal unit for certain property, thus recognizing the high degree of functional and economic integration of such property.

Unit valuation has also been described as follows:

> As its starting premise, the [unitary valuation] concept assumes that it is meaningless to consider the value of a mile of track, a substation, or a reel of cable standing apart from the entire operating system. The unit value of the enterprise may be either more or less than the total value of the individual assets making up the whole. Presumably, if each asset were sold separately, the total price received would be substantially less than the value of the enterprise as a going concern. This becomes more apparent when it is considered that ten miles of underground cable has a questionable worth, other than a minimal scrap value, if there is no generating plant at one end to provide electricity and no source at the other end to receive electrical energy. Similarly, fifty miles of railroad track, standing alone, are of questionable utility without the rest of the system.[24]

THEORETICAL BASIS

An examination of the theoretical rationale underlying the determination of the appraisal unit in general also reveals the underpinning for the principle of unit valuation used in the valuation of public utility property.

[24] Louis G. Bertane, *The Assessments of Public Utility Property in California*, 20 UCLA L. Rev. 419.

A market situation contains two primary attributes: a sale price *and* a unit of property that is sold. Given the market value standard of property tax assessment, it is logical and theoretically appropriate to think of the proper appraisal unit as a market unit. Indeed, for most types of property, assuming a relatively active market, the proper appraisal unit, or unit to be valued, is revealed by the market itself. The market provides the benchmark for determining the unit of property to be valued. For example, in the market for single-family homes the unit traded is the land *and* the improvement—the lot *and* the structure. The typical buyer or seller does not ascribe separate values to the lot and the improvement and sum them; they sell together as a market-defined unit. Further,

> [I]t would be meaningless to say that the buyer paid a certain percentage of the total price for the house and the remainder for the lot, just as it would be meaningless to say that the buyer paid a certain amount for the plumbing, a certain amount for the wiring, a certain amount for the foundations and a certain amount for the front door. The point is that the buyer bought the house and lot *as a unit* and there is no logic to any further distinctions. [Emphasis retained.][25]

The question remains, why do buyers and sellers of houses think in terms of the whole and not the parts? The answer, which is the theoretical underpinning of the appraisal unit concept, is because of the close functional relationship among the parts constituting the unit:

> *Why* does the buyer [and seller] of a house think in totals rather than fractions? The answer is clearly that the roof has almost no value without the walls that support it, the walls have almost no value without the foundations which support them, and the foundations have almost no value without the land which supports them.… *The individual parts of this house and lot perform cooperative functions*.… [I]t is equally true that the many operating parts of a complex railroad system, telephone company or gas and electric enterprise perform cooperative functions. For the same reason they must be valued as an entity rather than as a collection of pieces. [Emphasis retained.][26]

This single criterion of functional integration, however, is not adequate in and of itself. In a highly integrated and interdependent economy it is difficult to establish absolute functional boundaries. Functional integration must be combined with an obvious characteristic of the market situation—ownership:

> A sale represents a transfer of ownership and in normal circumstances the seller of a piece of property cannot market the property unless he owns it.… [T]he valuation unit may not extend beyond the boundaries of the unit of ownership, if

[25] California Legislature, 1953 Regular Session, Report of the Senate Interim Committee on State and Local Taxation, Part Six, "Property Assessments and Equalization in California," (Sacramento: California Legislature, 1953) 37. [Hereafter "Senate Interim Committee Report."]
[26] Senate Interim Committee Report, 38

> only because the ownership unit determines the maximum unit of marketability and marketability is an essential element in the concept of market value.[27]

Thus, from a theoretical perspective, the principle of unit valuation holds that the unit of property appropriate for the estimation of a market value should include all property items that are *functionally related* and within *common ownership*.

LEGAL BASIS

Several court cases have addressed the unit valuation of public utility property. In *Southern California Telephone Company* v. *Los Angeles County,* the court held that public utility property must be valued "as a whole" in order to ensure the assessment of those values that "cling to the entire property as a unit" and to ensure uniform assessment of public utility property.

> [T]he power to assess public utility property is placed exclusively in the hands of the Board of Equalization as a sole, central assessing agency. This is significant, because it is the common function of central assessing agencies to evaluate such property as a whole in order to assure the assessment of those values which cling to the entire property as a unit, and in order to assure the assessment of the same type of property at uniform value throughout the state. These are the reasons for central assessment of appellant's property as distinguished from local assessment thereof in all of the fifty-eight different counties. [28]

And in *ITT World Communications, Inc.* v. *City and County of San Francisco* (1985) 37 Cal.3d. 859 (also cited in *GTE Sprint Communications Corp.* v. *County of Alameda* (1994) 26 Cal.App.4th 992):

> One of the primary objectives of the system of unit taxation of public utility property is to ascertain and reach with the taxing power the entire real value of such property. [Citations.] It has long been recognized that "public utility property cannot be regarded as merely land, buildings, and other assets. Rather, its value depends on the interrelation and operation of the entire utility as a unit. Many of the separate assets would be practically valueless without the rest of the system. Ten miles of telephone wire or one specially designed turbine engine would have a questionable value, other than as scrap, without the benefit of the rest of the system as a whole." [Citation.] Unit taxation prevents real but intangible value from escaping assessment and taxation by treating public utility property as a whole, undifferentiated into separate assets (land, buildings, vehicles, etc.) or even separate kinds of assets (realty or personalty).

The United States Supreme Court has also consistently upheld the legal validity of unit valuation by central assessing authorities. The method has been challenged by taxpayers on several

[27] Senate Interim Committee Report, 40.
[28] *Southern California Telephone Company* v. *Los Angeles County* (1941) 45 Cal. App 2d. 111

grounds, including uniformity of taxation in regard to state versus local assessment; assessment of intangible value; burden on interstate commerce; and assessment of extrastate property. Notable cases addressing such matters include the following; *State Railroad Tax Cases* (1875) 92 U.S. 185; *Adams Express Co.* v. *Ohio State Auditor* (1899) 166 U.S. 185; *Cleveland, Cincinnati, Chicago & St. Louis Railway* v. *Backus* (1893) 154 U.S. 439; and *Norfolk & Western Railway* v. *Missouri State Tax Commission* (1968) 390 U.S. 317.

Finally, section 723 authorizes the Board's use of the principle of unit valuation:

> The board may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in a primary function of the assessee. When so valued, those properties are known as "unitary property." Property of an assessee not valued through the use of the principle of unit valuation are [sic] known as "nonunitary property."

ADJUSTMENTS WHEN USING THE PRINCIPLE OF UNIT VALUATION

The next chapter discusses the approaches to value as they are applied in unit valuation. Noted here, however, is that several adjustments may be required to the initial unitary value indicator prior to arriving at the final unitary value indicator and the allocation of the unit value. These adjustments can be divided into two general types. The first type is required to adjust the initial value indicator so that it reflects only the value of the unitary property; the need for and nature of this adjustment depends on the approach to value that is used. The second type is required to adjust the unit value indicator so that it does not contain nontaxable property—either nontaxable tangible property or intangible assets or rights.

CLASSIFICATION OF STATE ASSESSED PROPERTY

In California, state assessed property is classified into one of four categories: (1) unitary property, (2) nonunitary property, (3) operating nonunitary property, and (4) nonunitary rail transportation property. Stated slightly differently, unitary property and three types of nonunitary property constitute the classifications. Classification affects the way property is valued and, as explained in Chapter 5, the way property value is allocated.[29]

UNITARY PROPERTY

The general definition of unitary property is property owned or leased by the state assessee and used in its primary operations as part of the state assessee's integrated system.

More specifically, within the general definition the following types of property are classified as unitary: (1) special-purpose or industry-specific property that is leased by the state assessee; (2) property leased by a state assessee, used in the assessee's primary operations, and assessed to the

[29] Appendix C contains tables showing the Board's classification codes for various types of property.

assessee (including taxable possessory interests); (3) property owned and held for future use in the primary operations of the assessee if there is a documented plan for the property's future use and the property is carried in a future use operating account; and (4) property that is owned and used to protect and support other unitary property—due to locational or physical characteristics or other factors. Under the principle of unit valuation, unitary property is valued as a single unit.

Examples of Unitary Property:

- Land, improvements, and personal property owned or leased by a state assessee and used in its primary operation of transportation of freight by rail; gas or fluids by pipeline, canal or ditch; generation, transmission or distribution of electricity; or transmission of information by cellular, paging, or telephone.
- Vacant land that is considered necessary to protect areas utilized in the primary operations of the assessee (e.g., buffer areas required for nuclear power plants or gas storage reservoirs, slide areas near railroad tracks, drainage ditches, etc.).
- Vacant land that is located in landlocked areas totally surrounded by sets of railroad tracks or areas adjacent to rights-of-way that are too narrow to be developed to another use.
- Property that the state assessee had acquired for use in its primary operations but now has a secondary use (e.g., areas beneath tower lines which are farmed, used for parking or storage; areas above gas storage reservoirs which are farmed).
- Railroad rights-of-way acquired by congressional grant or franchised by a governmental agency.
- Utility and railroad easements for rights-of-way.
- Railroad property that is leased to agents of the railroad, who manage the property in a rail transportation use (e.g., intermodal container yards).

NONUNITARY PROPERTY

Nonunitary property is property that is owned by a state assessee but not used in the assessee's primary operations. Nonunitary property is valued separately and apart from unitary property (i.e., not valued as part of the unit).

Examples of nonunitary property:

- Property owned by and assessed to a state assessee, but leased to others.
- Property owned by a state assessee and not used in its primary operations.
- A railroad right-of-way that has had the track removed or has been abandoned (includes the land under the track that has been severed from the operating portion).
- Property used by others without a formal lease (e.g., encroached upon and used for storage, parking, or growing of trees, vines, or crops).

OPERATING NONUNITARY PROPERTY

Operating nonunitary property is specifically defined in section 723.1:

> Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the board considers not part of the unit in the primary function of the assessee. This section does not apply to state-assessed property of regulated railway companies….

Section 723.1 essentially provides discretion to the Board. The Board may classify property as operating nonunitary that others classify as unitary. Operating nonunitary property is valued separately and apart from unitary property (i.e., not valued as part of the unit).

Example of operating nonunitary property:

- State assessee-owned property that is included in its rate base but is classified as nonunitary (e.g., land on which a substation has been removed but it still is carried in the rate base) [but excludes railroad property.].

NONUNITARY RAIL TRANSPORTATION PROPERTY

Nonunitary rail transportation property is property owned by a railroad company that is used in rail transportation operations, but is nonetheless valued separately and apart from unitary property (i.e., not valued as part of the unit).

Examples of nonunitary rail transportation property:

- Railroad property leased to Amtrak, Caltrans, or transit districts.
- Railroad property leased to others, whose primary use of the property involves the receipt and/or shipping of products or raw material by rail (e.g., lumber yards, liquid tank car receivers, intermodal container yards, automobile loading-unloading facilities, etc.).
- Railroad property owned by and assessed to a state assessee, but leased to others whose primary operation is that of freight transportation (however, state assessee-owned property leased to others but not used for freight transportation is classified as nonunitary.).
- Railroad land leased at a rent substantially below market (e.g., an accommodation lease), where freight or products are received or shipped frequently.
- Station grounds used for passenger parking (e.g., Amtrak, Caltrans, Transit districts, etc.).

CHAPTER 4: UNITARY VALUE INDICATORS

Value indicators are the evidences of market value prepared by the appraiser in support of the final value conclusion. Each year, as prescribed in Rule 902, staff develops unitary value indicators that are used by the Board in reaching its unitary value determinations. Staff also recommends annual values for state assessees' other property located in California, that is, nonunitary property, operating nonunitary property, and nonunitary rail transportation property.

Under Rule 3 there are five indicators of market value, or value approaches, one or more of which must be considered in property tax valuation:

~~a)~~1. The price or prices at which the subject property or comparable properties have recently sold (the comparative sales approach).

~~b)~~2. The prices at which fractional equity interests in the subject property or comparable properties have recently sold, and the extent to which such prices would have been increased had there been no prior debt claims on the assets (the stock and debt approach).

~~c)~~3. The cost of replacing reproducible property with new property of similar utility, or of reproducing the property at its present site and at present price levels, less the extent to which the value has been reduced by depreciation (the replacement and reproduction cost approaches, respectively).

~~d)~~4. If the income from the property is regulated by law and the regulatory agency uses historical cost or historical cost less depreciation as a rate base, the amount invested in the property or the amount invested less depreciation computed by the method employed by the regulatory agency (the historical cost approach).

~~e)~~5. The amount that investors would be willing to pay for the right to receive the income that the property would be expected to yield, with the risks attendant upon its receipt (the income approach).

Related specifically to the valuation of unitary property, staff of the Board's Valuation Division has recently developed and published *Unitary Valuation Methods*, a publication that describes the valuation models (i.e., valuation approaches) used by staff in its preparation of unitary value indicators. In addition, as also prescribed in Rule 902, Valuation Division staff conducts and publishes an annual capitalization rate study that develops capitalization rates used in the Board's capitalized earnings ability model.[30]

Descriptions of the valuation models contained in Unitary Valuation Methods and the methods of capitalization rate derivation described in the annual capitalization rate study are not repeated in this manual; instead, the reader is referred to those publications. The reader also is referred to Assessors' Handbook Section 501, *Basic Appraisal*, and Section 502, *Advanced Appraisal*,

[30] Both *Unitary Valuation Methods* and the annual capitalization rate study are available from the Board.

publications containing discussions of general valuation principles and methods, much of which is generally applicable to the valuation of public utility property.

CHAPTER 5: ALLOCATION OF UNITARY VALUE

If the unit value contains the value of unitary property located outside California, a portion of the multistate unit value first must be allocated to California. The allocation of unit value between or among states is called interstate allocation. The unitary value indicators prepared for the Board by staff are post-interstate allocation; that is, staff has already made any necessary interstate allocations.

California's portion of the multistate unit value must also be allocated among the state's local tax jurisdictions. The allocation of unit value within a state is called intrastate allocation. If all of a state assessee's unitary property is located in California, obviously no interstate allocation is required.

The values for all state assessed property appear on what is called the "board roll." Under section 756, on or before each July 31, the Board must provide each county auditor with a roll showing the values for all state assessed property located in his or her county. The state assessments are levied, and the corresponding property taxes collected, at the county level.

Unfortunately, no method of allocation can be theoretically satisfying from a valuation perspective if one accepts the principle of unit valuation. The allocation of a unit value, which is an attempt to obtain separate market values for the component parts of an operating unit, contradicts the principle of unit valuation. If it is not possible to add up the separate values of the component parts of an operating unit to determine the value of the unit—in essence, the principle of unit valuation as it is applied to public utility property—then it is equally impossible to determine the separate market values of the component parts by breaking up the value of the unit. Unit valuation is thus logically inconsistent with any method of value allocation that purports to be according to market value.

Theoretical problems aside, the need for inter- and intrastate allocation, and hence the need for an allocation method, is based on clear legal requirements. First, under federal law California, like all other states, has no authority to tax property located outside its boundaries. Second, section 14 of article XIII of the California Constitution requires that "All property … shall be assessed in the county, city, and district in which it is situated."

The result is that allocated amounts, in both inter- and intrastate allocation, in a strict sense do not represent market values; rather, they are portions of the unit value allocated in an equitable and systematic manner to allow assessment and taxation by the appropriate legal jurisdiction.

The following sections describe, in general terms, the Board's procedures for the inter- and intrastate allocation of a unit value. These procedures, although based on the same concepts, vary by industry and by whether the allocation is inter- or intrastate. A concluding section also

briefly describes the Board's tax-rate area system, the means by which all property in California is assessed according to its situs.[31]

INTERSTATE ALLOCATION

BASIS FOR INTERSTATE ALLOCATION

Both the National Association of Tax Administrators (NATA) and the Western States Association of Tax Administrators (WSATA) have made recommendations regarding the interstate allocation of unit value. In 1949, NATA, based on work by its Committee on Railroad Allocations, adopted an allocation formula for railroads; and in 1960, WSATA, based on work by its Committee on Allocation of Public Utilities, recommended allocation formulas for other types of utility property. In general, the Board follows NATA's and WSATA's recommendations regarding interstate allocation methods.

The Board considers several general principles in its allocation criteria. Largely derived from NATA and WSATA, they include the following:

- Allocation percentages should not total more or less than 100 percent for all states.
- Allocation factors should reflect the quantity of property in each state.
- Allocation factors should be based on readily available, objective data.
- Allocation factors should not be based on data that are the result of a prior allocation.
- The resulting allocation should be "fair and equitable."
- The allocation method should consider administrative feasibility and convenience.
- As much as possible, the allocation should divide the unit value in proportion to the contribution made by the unitary property in each state to the unit value (despite the theoretical difficulty related to this).

In practice, the interstate allocation of unit value is based on an allocation factor or, more typically, a combination of allocation factors. An interstate allocation factor is intended to measure the importance of a given variable in a state relative to its importance in the unit as a whole. For example, if the variable is the historical cost of the property, the historical cost of the

[31] A few points about interstate allocation that are well known to those involved but perhaps not obvious to others: (1) Each state estimates its own unit value, and each state may define the unit slightly differently. Further, tax law may vary between states as to what is or is not subject to ad valorem property tax. So, if a given assessee operates in, say, three states, three unit values will be estimated. (2) Prior to the efforts of NATA and WSATA, there was only limited agreement regarding allocation formulas. This meant that the total percentages allocated by the respective states could sum to significantly more or less than 100 percent. This problem has been largely rectified. (3) There is an abundance of federal court cases concerning allocation of various types of interstate property. In general, the federal courts will strike down allocation systems they deem unreasonable. Beyond that, the federal courts have declined to interfere with a state's allocation system that is based on some reasonable relationship to the rights and benefits of having the property located in the state. There is no federal requirement that the total of all state assessments must equal (or cannot exceed) 100 percent.

property in a given state is divided by the historical cost of all the property in the unit. The quotient is an allocation factor based on historical cost. When the allocation factor is multiplied by the unit value, the product is the state's portion of the unit value.

Often, two or more allocation factors, reflecting different allocation variables, are combined. When factors are combined, weights are assigned to each factor. The result is a composite factor—a weighted average of the individual factors—that is then used for allocation. Different composite factors can be developed using different individual factors and different weightings. The calculations required to arrive at a composite allocation factor are often called the "allocation formula."

Individual allocation factors are generally based on property, use, or revenue variables. Property factors are based on the visible, physical assets in the unit, such as cost (original, or historical; reproduction; or replacement), wire-miles, pole-miles, track-miles, distribution mains, etc. Use factors are based on some type of physical activity that takes place, such as car-days, car- or locomotive-miles, ton- or passenger-miles, barrel-miles, MCF-miles (MCF = thousand cubic feet), originating- or terminating-tons, and kilowatt hours-sold or kilowatt hours-generated. Revenue factors represent some measure of earnings, such as gross revenue and net operating income. Revenue factors are sometimes interpreted as measures of "economic use" and are considered as part of the use category.

The specific procedures used in interstate allocation vary by industry, but the methods are similar. The Board's procedures for the interstate allocation of unit values are described briefly below, by industry group.

INTERSTATE ALLOCATION PROCEDURES

Electric

Electric utility companies often have unitary property used for the generation, sale, transmission, and distribution of electricity—or a combination of these operations—in more than one state. For the interstate allocation of an electric company's unit value, the Board follows WSATA's interstate allocation formula for electric utilities.

The WSATA formula allocates unit value on the basis of historical cost modified by other allocation factors. Separate allocations are made according to defined operating segments: electric production property, electric distribution property, and remainder of property. Allocation factors and factor weightings used for the three defined operating segments are as follows:

- Electric production property: 75 percent historical cost; 10 percent kilowatt capacity; and 15 percent kilowatt hours generated.
- Electric distribution property: 50 percent historical cost; 10 percent kilowatt-hours delivered and sold; and 40 percent for revenues from these kilowatt-hours.
- Remainder of property: 100 percent historical cost.

Thus, the value of the electric production segment is allocated using a composite allocation factor composed of three individual allocation factors—historical cost, kilowatt capacity, and kilowatt hours generated; the value of the electric distribution segment is allocated using a composite allocation factor composed of three individual allocation factors—historical cost, kilowatt hours delivered and sold, and revenue; and the value of the remainder of the property is allocated using a single allocation factor—historical cost.

These three factors are then multiplied by allocated percentages of the unit value for each operating segment; this percentage allocation is based on the historical cost of the property in each segment. The sum of these three products is the final allocation factor for California; when this factor is multiplied by the entire unit value, the result is the portion of the unit value assessed in California.

Telecommunication

A telephone company differs from other utility companies because of the structure of the telephone industry. Typically, a telephone company can only operate, or operate most efficiently, when connected to other telecommunications systems. There is a high degree of system interdependence.

Telephone companies can be classified into three types: local exchange, interexchange, and wireless. Local exchange companies provide services in a defined geographic area, usually within a single state. In the case of multistate local exchange companies operating in California, the geographic area served, amount of property, and revenues in California generally are very limited. Nonetheless, in such cases, the interstate allocation of the unit value is still required. Typically, the Board makes this allocation using a single allocation factor based on historical cost.

Interexchange companies provide telephone services from one local exchange to another local exchange. Often, an interexchange company provides services in more than one state. The Board's interstate allocation of the unit value of an interexchange company is also made using a single allocation factor based on historical cost.

A wireless telephone company provides mobile telecommunication services through its own facilities, facilities owned by other wireless companies, and facilities owned by local and interexchange companies. Wireless companies own or lease sites, towers, and antennas in numerous counties throughout the state and may own or lease property in other states. For wireless companies, the Board makes its interstate allocation of unit value using an allocation factor based on gross revenue.

Pipeline

Pipeline companies own property used in the distribution of oil, natural gas, and other products in a liquid state; their operations are frequently interstate. The property involved can be divided into two categories: the pipeline itself and "other property," which includes buildings, gathering

systems, pumping stations, materials and supplies, and other assets that are not part of the pipeline itself but are used in the pipeline company's operations.

With pipeline companies, it is practically impossible to arrive at earnings estimates that can be ascribed to property on a state-by-state basis. Barrel-miles or MCF-miles are reasonable substitutes for earnings. Other appropriate allocation factors are those based on original or historical cost and originating and terminating barrels or MCF.

The Board typically uses a slightly modified form of the WSATA recommended allocation formula that includes the historical or original cost of pipeline and other property, barrel- or MCF-miles, and originating and terminating barrels or MCP as allocation factors, weighted as follows:

- Historical or original cost: 75 percent
- Barrel- or MCF-miles: 20 percent
- Originating and terminating barrels or MCF: 5 percent

When originating and terminating barrels or MCF data are not available, Board practice has been to modify the above formula by giving a 75 percent weighting to historical or original cost and a 25 percent weighting to barrel- or MCF-miles.

Railroad

For the interstate allocation of railroad unit value, the Board uses a modified version of the NATA formula. The modifications:

- Undepreciated cost is used because cost data are readily available and estimates of depreciation are not necessary.
- Rolling stock and other mobile equipment costs are excluded because they are based on allocations.
- Miles of way and yards of tracks are included to reflect terminal activity in California.
- Fixed weightings are assigned to the property, line haul, and terminal factors because the Surface Transportation Board (formerly, the Interstate Commerce Commission) no longer provides the expense data necessary to calculate weights.

The Board uses a composite allocation factor to allocate railroad unit value. The individual allocation factors and their weightings in the composite factor are as follows:

- Cost (Surface Transportation Board form R-1), a property factor: 40 percent.
- Revenue ton-miles, a line-haul factor: 45 percent.
- Sum of tons of originating and terminating freight, tons received and delivered, and miles of yard and way switching track, a terminal factor: 15 percent.

The Board uses data from the Surface Transportation Board to calculate the individual allocation factors.

INTRASTATE ALLOCATION

BASIS FOR INTRASTATE ALLOCATION

Except for railroad property and property subject to subdivisions (i) and (j) of section 100, both of which are discussed in sections below, the intrastate allocation of unit value is to the county level only; the county auditor is responsible for further allocation of this value among the county's local tax jurisdictions. As stated in section 745:

> "The assessment of the unitary and operating nonunitary property of an assessee shall be allocated … among the counties in which parts of the unitary and operating nonunitary property are situated." [32]

Section 745 provides broad discretion to the Board regarding the method of allocation. The Board's primary objective is to use an allocation method resulting in an allocation of value to each county that is a reasonable estimate of the allocated part's proportionate value contribution to the intrastate unit value. In other words, the objective is for an allocation to each county that is as closely related as possible to the value of each assessee's unitary property in the county. Excluding the exceptions discussed below, intrastate allocation procedures, unlike interstate procedures, do not vary significantly by industry.

INTRASTATE ALLOCATION PROCEDURES[33]

Unitary Land

Board appraisers estimate the market values of each state assessee's unitary land parcels for each lien date, using generally accepted appraisal methods. The total unitary land value for each state assessee is the sum of the values of the assessee's unitary land parcels. This total unitary land value is allocated to each county based on situs (i.e., to each county's general countywide tax-rate area).

Unitary Property Other Than Land

The value of each assessee's unitary property other than land remains to be allocated. For each assessee, this amount is the assessee's total unit value less the value of the assessee's unitary land as determined in the section above. This is often called the "net unit value." The allocation of net unit value to each county is further segregated into improvements and personal property.

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[32] The county auditor's intracounty allocation of unitary value among the myriad local tax jurisdictions must follow the formula prescribed in section 100.

[33] Again, the discussion in this section excludes railroad property and property subject to subdivisions (i) and (j) of section 100.

For the property of the seven largest state assessees and for all pipeline property, the intrastate value allocation of the net unit value is based on reproduction cost new less depreciation (ReproCNLD). The allocation factor for a given assessee's property in a given county is the ratio between current ReproCNLD of the assessee's property in that county to current ReproCNLD of the assessee's net unit value.

For the remaining state assessees, those other than the seven largest, the allocation method is analogous, but the intrastate allocation factor is based on historical cost rather than ReproCNLD.[34]

Unitary property other than land includes property that is identifiable by location—buildings, substations, equipment, furniture, etc. For each property item, the assessee reports the original cost by acquisition year, and the location by general countywide tax-rate area (i.e., to the county level).

Also included in unitary property other than land are gas transmission and distribution mains, electrical transmission and distribution lines, telephone wires and cables, canals, pipelines, etc., all examples of a type of unitary property called "continuous structures." For intrastate allocation, the Board treats continuous structures in the same manner as property identifiable by location. For each portion or segment of a continuous structure, the assessee reports its original cost by acquisition year and its location by general countywide tax-rate area (or, if not so reported, Board staff will allocate the "continuous structures" by county).

Intrastate Allocation Summary

The guiding principle of intrastate allocation is location, or situs, with value allocated to situs using allocation factors based on either ReproCNLD or historical cost. Here is a two-step summary:

1. Board staff estimates an assessee's unitary land value and allocates this value by location to each general countywide tax-rate area. The value of unitary property other than land, the "net unit value," remains to be allocated. For each assessee, this is the assessee's total unit value less the assessee's total unitary land value.[35]

2. For the seven largest state assessees and all pipeline assessees, the value remaining, the net unit value, is allocated to the county level using an allocation factor based on ReproCNLD. For all other assessees, the remaining unit value is allocated to the county level using an allocation factor based on historical cost. Allocated values are differentiated by "improvements" and "personal property." The sum of the allocated values for each county equals 100 percent of the Board-adopted unitary value.

[34] We have eliminated one slight complication. "Materials and supplies" are typically directly deducted from the assessee's total unit value and allocated to each county by situs based on their full reported cost. The "net unit value" referred to above is thus actually the total California unit value less the value of unitary land less the value of deducted materials and supplies. The amount of materials and supplies is generally not significant relative to the total allocated value.

[35] Intercounty pipeline *land and rights of way*, however, are locally assessed.

EXCEPTIONS TO GENERAL INTRASTATE ALLOCATION METHOD

Section 100.9

Section 100.9, effective beginning with the 2003-2004 fiscal year, requires that the assessed value of electric generation facilities assessed by the board pursuant to section 721.5 must be allocated exclusively to the county in which the facility is located and that the revenues derived from the assessment of this property must be allocated in the same percentage shares as revenues derived from locally assessed property among the jurisdictions in which the property is located. Section 100.9 states:

> (a) Notwithstanding any other provision of law and except as provided in subdivision (b), for the 2003-04 fiscal year and each fiscal year thereafter, all of the following apply:
>
> (1) The property tax assessed value of an electric generation facility that is assessed by the State Board of Equalization shall be allocated entirely to the county in which the facility is located, and shall be allocated to that tax rate area in the county in which the property is located.
>
> (2) The tax rate applied to the assessed value allocated pursuant to paragraph (1) shall be the rate calculated pursuant to Section 93.
>
> (3) The revenues derived from the application of the tax rate to the assessed value allocated to a tax rate area pursuant to paragraph (1) shall be allocated among the jurisdictions in that tax rate area, in those same percentage shares that property tax revenues derived from locally assessed property are allocated to those jurisdictions in that tax rate area, subject to any allocation and payment of funds as provided in subdivision (b) of Section 33670 of the Health and Safety Code, and subject to any modifications or adjustments pursuant to Sections 99 and 99.2.
>
> (b) Subdivision (a) does not apply to the assessed value or the revenues derived from that assessed value from either of the following:
>
> (1) An electric generation facility that was constructed pursuant to a certificate of public convenience and necessity issued by the California Public Utilities Commission to the company that presently owns the facility.
>
> (2) An electric generation facility that is owned by a company that is a state assessee for reasons other than its ownership of the generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.

Railroad Property

Railroads are an exception to the general intrastate allocation method based on ReproCNLD or historical cost. Section 100.1 governs the intrastate allocation of the value of the property of

regulated railway companies. The unit values of railroad company property, unlike the unit values of other public utility property, are allocated to specific county tax-rate areas, not to the general, countywide tax-rate area. Also, the unit values of railroads are allocated based on estimated weighted track mileage in each tax-rate area, using a 1987 base year. Track mileage is weighted to reflect the relative importance of track type (e.g., mainline, branch, and other track). Further allocation among land, improvements, and personal property is also proportional to values from the 1987 base year.

Other Property Allocated to Specific Tax-Rate Area

Another exception to the general intrastate allocation method described above is property specifically described in subdivisions (i) and (j) of section 100 (sometimes called "Hannigan property," after the legislator). These subdivisions pertain to property that is undeveloped, owned by a public utility, and located within a city, county, or city and county that has adopted a resolution making the property subject to a development plan or agreement. A copy of the resolution also must have been transmitted to the Board before specified dates. The value of this property also must be allocated by specific tax-rate area rather than general countywide tax-rate area.

State assessees report such property's historical, or original, cost by acquisition year and its location by specific local tax-rate area. The value of this property is directly allocated to the specific tax-rate area within which the property is located, using an allocation factor based on historical cost. As described earlier, the value of all other unitary property in a county is allocated only to the countywide tax-rate area.

STATE ASSESSED PROPERTY NOT SUBJECT TO UNITARY ALLOCATION

The preceding sections described how the value of unitary property was allocated to the board roll and hence, eventually, to each local assessment roll. The remaining discussion focuses on how the rest of state assessed property—that is, nonunitary property, operating nonunitary property, and nonunitary rail transportation property—is assessed and enrolled.

Nonunitary property is valued separately from the unit and its value is enrolled to the board roll by specific county tax-rate area. The value of nonunitary property is not subject to the intracounty allocation performed by county auditors under section 100.

Operating nonunitary property is valued separately from the unit but enrolled to each county's general countywide tax-rate area by situs (actually to a special, countywide tax-rate area reserved for it). Operating nonunitary property is subject to the intracounty allocation performed by county auditors. So, it receives a hybrid treatment (i.e., separately valued, but with value allocated).

Nonunitary rail transportation property is valued separately from the unit and its value is enrolled to the Board roll by specific tax-rate area. The value of nonunitary rail transportation property is not subject to the intracounty allocation performed by county auditors under section

100. The value of this type of property receives the assessment ratio treatment described in an earlier section relating to the Railroad Revitalization and Regulation Reform Act (4-R Act). Excluding this treatment under the 4-R Act, nonunitary rail transportation property is treated exactly as nonunitary property.

BOARD'S TAX-RATE AREA SYSTEM

The Board's tax-rate area system facilitates compliance with the constitutional requirement that all taxable property be assessed according to situs. The tax-rate area system assigns a unique tax-rate area number to every geographical area in the state that corresponds to a unique combination of overlapping tax levies made by local revenue districts (e.g. cities, school districts, special districts). A general, countywide tax-rate area number is also part of the system.

A tax-rate area number contains six digits. The first three digits refer to primary areas and the second three digits to secondary areas. The primary-area digits identify incorporated cities and school districts in unincorporated areas of a county. The secondary-area digits identify all other revenue districts within a given primary-area digits sequence. Since the geographic boundaries of these districts do not conform to those of the primary area numbers, subdivisions within the primary areas were created and numbered in ascending order beginning with "001."[36]

State assessed property is identified by "000" in the primary-area digits of the tax-rate area number; unitary and operating nonunitary property are identified by "001" in the secondary-area digits. State assessees generally report their unitary property by countywide tax-rate areas. The Board then assesses the unitary property to the respective countywide tax-rate areas (except for railroad property and property subject to subdivisions (i) and (j) of section 100) and delivers the portion of the Board roll pertaining to each county to the respective county auditor. As discussed above, nonunitary property and nonunitary rail transportation property are identified to the level of specific county tax-rate area.[37]

[36] Los Angeles County maintains its own five-digit numbering system, which does not completely differentiate cities from other districts.

[37] The Board's tax-rate area system is described in slightly greater detail in Assessors' Handbook Section 215, *Assessment Map Standards*.

CHAPTER 6: APPEALS OF STATE ASSESSMENTS

This chapter discusses appeals of state assessments. Under sections 731 and following, a state assessee or its designated representative may request a review of (1) the value of its unitary and/or nonunitary property and any related penalty assessments; (2) the allocation of the unit value of its unitary property among counties; and (3) the results of a Board audit resulting in escape assessments. The Board sits as the administrative appeals body for state assessments.[38]

This chapter begins with a brief discussion of the valuation process as it relates to appeals of state assessments. This is followed by a discussion of the appeals process, including petitions for filing an appeal, conduct of Board hearings, and further appeal rights of state assessees.[39] A brief discussion of the audit review process and escape assessments resulting from an audit concludes the chapter.

VALUATION PROCESS

Each year, the Board's Valuation Division prepares value indicators for state assessed property as of the January 1 lien date in that year, and submits its value indicators and value recommendations to the Board. For unitary property, values are established by the Board at public hearings in May. For nonunitary property, values are established by the Board at public hearings in June.

As discussed in Chapter 5, the Board allocates the unit value of a state assessee's unitary property and assigns the value of its operating nonunitary property to each county in which such property is physically located. All other state assessed property is assessed directly to the specific county tax-rate area in which the property is physically located. All assessments made by the Board appear on an annual Board-prepared assessment roll—the Board roll—that is sent to county auditors.

Assessee Review and Comment

Prior to the Board's annual valuation, a state assessee may review the staff's annual capitalization rate study and its work papers related to value indicators for *unitary* property.

The Board also provides a state assessee with the opportunity to make a presentation to the Board, either in person or in writing, regarding capitalization rates and other matters affecting the Board's valuation of its property. The Board holds public meetings in February and May for these purposes.

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[38] The Board also hears property tax appeals concerning assessments of taxable property owned by local governments outside their boundaries (section 11 property) and claims for the welfare exemption that have been denied by Board staff.

[39] The procedures and deadlines referenced in this text reflect all statutory amendments made under Stats. 2000, Chap. 647 (SB 2170), effective on January 1, 2001, to Revenue and Taxation Code sections 731, 732, 733, 746, 748, 749, 758 and 759.

Notification of Value

After the Board establishes annual values for all state assessed property, all state assessees are sent notices of assessment that also provide information on the procedure for appealing assessments.

Notices of assessment are mailed by June 1 for unitary property and by the last day of July for nonunitary property. A property's assessed value becomes final after July 20 and September 20 of the same calendar year in which the notice is provided for unitary and nonunitary property respectively, unless the assessee files a petition for reassessment.

After receiving the notice of assessment, a state assessee may obtain, by written request, a copy of the appropriate staff capitalization rate study and the final calculations of value indicators relevant to the property to which the notice pertains. If requested, this information must be provided to the assessee prior to the deadline for filing a petition for reassessment.

Tax Payment

Tax is payable to the appropriate county or counties in two installments on November 1 (payment deadline December 10) and February 1 (payment deadline April 10).

APPEALS PROCESS – ASSESSMENTS AND PENALTIES

The appeals process is the same for both unitary and nonunitary properties, unless noted otherwise. The four basic steps in the appeal of a value established by the Board are as follows:

1. File a petition for reassessment, a petition for reassessment and claim for refund, a petition for correction of an allocated assessment, or a petition for penalty abatement with the Board.

2. Submit the matter for hearing by the Board (if the assessee does not request an oral hearing, the Board will base its decision on the contents of the written petition and the written recommendation made by the Board's staff).

3. File a claim for refund with the county, if not previously filed with the Board (taxes must be paid to county or counties).

4. File an action in superior court (if claim for refund is denied).

Although the appeals process generally proceeds step-by-step, some steps may be combined or skipped, as explained in the following section.

PETITION FOR REASSESSMENT, PENALTY ABATEMENT, OR CORRECTION OF ALLOCATED ASSESSMENT

Petition for Reassessment or Petition for Penalty Abatement

For unitary property, a petition for reassessment may be filed no later than July 20. For nonunitary property, a petition for reassessment may be filed no later than September 20. For escape assessments, the date for filing a petition for reassessment shall not be less than 50 days from the date of mailing of the notice of value.

The petition for reassessment or the petition for penalty abatement must be in writing. The petition for reassessment must state:

- The name of the property owner;
- The assessee's opinion of the property's value; and
- The precise elements of the Board's valuation being contested.[40]

The petition for penalty abatement must present facts establishing that:

- There was a reasonable cause for the inaccurate or delayed filing;
- The problem occurred despite best efforts to file an accurate and/or timely statement; and
- The assessee did not intentionally neglect its filing obligations.

If the assessee wants to make an oral presentation before the Board, the request must be included in the petition. Otherwise, the Board will consider the merits of the written petition and the Board staff's written recommendation and make its decision at a public meeting (nonappearance agenda).

The petition may serve as a claim for refund of taxes to be paid on the assessment that is the subject of the petition. If the petition serves as a claim for refund, it should state this clearly.

The Board hears petitions for reassessment of unitary and nonunitary values or penalty abatement between the date a timely petition is received and December 31 of the same year. The Board must reach a decision on such petitions no later than December 31.

Petition for Correction of Allocated Assessment

No later than June 15, the Board must send each assessee a written notice of the allocated assessed values of the assessee's unitary property. An assessee may appeal the value allocation of its unitary property by filing a petition for correction of an allocated assessment. The deadline for filing a petition for correction of an allocated assessment is July 20. In the petition, the assessee must state the specific reasons on which the claim for correction or adjustment of the

[40] Appraisal reports, financial studies, and other materials relevant to value must be included and submitted with the petition for both reassessment and for penalty abatement.

allocation is grounded. Under a petition for correction of an allocated assessment, the assessee may not contest the total value of its unitary property; only the allocation of the unit value may be contested. The petition may serve as a claim for refund of taxes to be paid on the assessment that is the subject of the petition. If the petition serves as a claim for refund, it should state this clearly.[41]

BOARD HEARING

The Board hearing gives the assessee the opportunity to summarize and emphasize the points supporting its position. An assessee may present any relevant evidence, provided it is the sort of evidence generally relied upon by responsible persons in establishing value for similar properties.

At the hearing, the Board will generally consider only the values, issues, or precise elements set forth in the petition. However, the Members may inquire into relevant new matters and give the assessee or the Board staff an opportunity to respond.

Burden of Proof

Ordinarily the assessee has the burden of proof regarding any disputed facts. In a hearing on a petition for abatement of a penalty for failure to file an accurate and/or timely property statement, under section 830 the assessee must establish to the Board's satisfaction that:

- There was reasonable cause for the inaccurate or delayed filing;
- The problem occurred despite best efforts to file an accurate and/or timely statement; and
- Filing obligations were not intentionally neglected.

In a hearing on a petition for abatement of other penalties, however, Board staff bears the burden of proof.

Conduct of the Hearing

A Board hearing generally consists of the assessee's unsworn presentation, presentations by Board staff (usually an appraiser and an attorney), and, if necessary, testimony by witnesses. If the assessee requests, the Board will conduct a formal evidentiary hearing in which witnesses testify under oath or affirmation.

A hearing usually proceeds as follows:

1. A Board staff attorney introduces the case by summarizing the facts, applicable law, and issues involved. If an assessment is at issue, the attorney will offer into evidence the

[41] Under sections 5096 through 5097.2, a claim for refund of taxes paid more than once or erroneously or illegally collected or levied must be made in writing, specifying the grounds on which the claim is founded, and must be filed within four years after making the payment sought to be refunded, or within one year after the mailing of the tax collector's notice of overpayment, whichever is later.

Board's determinations of value. Following this introduction, the staff attorney will introduce the assessee or the assessee's representative.

2. In a case in which the assessee bears the burden of proof, the assessee or the assessee's representative states its position regarding the facts and applicable law and presents its evidence.

3. After the assessee's presentation, the Board staff attorney presents arguments based on the staff's evidence and responds to the assessee's arguments.

4. The assessee is given the opportunity to reply to the Board staff presentation.

5. If a witness is called, the assessee or the assessee's representative may ask questions of the witness without interruption, as long as the testimony is competent and relevant. When the assessee completes the examination of the witness, a Board Member (or, at the discretion of the Board Chair, the Board staff attorney), may examine the witness.

6. Finally, the Board Members may ask each party questions about the petition, the facts, or the law.

Admission of Evidence

For evidence, such as appraisal reports, financial studies, and other materials relevant to the value of the property, to be admitted, Board rules require that it be submitted to the Board with the petition.

The Board is not bound by the formal rules of evidence used in court. Board Members may admit all relevant evidence, including affidavits or hearsay, if it is the sort of evidence responsible persons rely upon in the conduct of serious affairs. While the Board follows a liberal standard for admission of evidence, the Board may exercise discretion when determining what weight to assign to evidence, considering any objections to its admission and/or comments on its weakness. The Board my refuse to admit evidence that it considers irrelevant, untrustworthy, or too repetitive.

Board Determination

All Board determinations are made at public hearings. If an oral hearing is held, the Board may take one of the following actions:

- Order the matter to be taken under submission;
- Decide the matter at the conclusion of the hearing day; or
- Order the matter to be taken under submission, and allow the assessee and/or the Board staff more time to submit specific information.

Generally, petitions taken under submission by the Board, and those for which oral hearing has been waived, are put on a nonappearance agenda and voted on during a regularly scheduled

Board meeting. If the petition is on the nonappearance agenda, the assessee normally will not be informed of the date of the Board meeting at which the matter will appear on the agenda.

When a decision is reached, the Board sends a written notice of decision, and, if requested in the petition, written findings and decision. The Board's decision is final. A petition will not be reconsidered or reheard.

FILING A CLAIM FOR REFUND

An assessee may file a claim for refund of tax to be paid or paid on a contested assessment or allocation. There are two different procedures, depending on whether the petition itself is intended to serve as a claim for refund.

Claim for Refund Made With Original Petition

As discussed above, the petition may also serve as a claim for refund, provided that the petition so states. If the Board denies the petition and, hence, the claim, then upon payment of tax to the county or counties, the assessee may proceed directly to file an action in superior court for a refund of the tax.

Subsequent Claim for Refund

If the Board denies a petition that does not also serve as a claim for refund, after the assessee has paid the tax, the assessee may file a written claim for refund with the county or counties where the property is located. The claim must be filed:

- Within four years from the date of payment of the tax; or
- Within one year from the mailing date of a notice or overpayment, whichever is later.

The claim for refund must state all of the reasons the assessee believes the assessment or allocation is incorrect. The county board of supervisors will consider the claim and mail its decision to the assessee. If the county rejects all or part of the claim for refund, or does not send a decision notice within six months of the date of the claim is filed, the assessee may proceed to file an action in superior court for a refund of the tax.

FILING AN ACTION IN SUPERIOR COURT

After the Board or the county has rejected a claim for refund (or has not sent a decision notice within six months of claim filing), the assessee has exhausted its administrative remedies and may bring an action in superior court for refund of the tax.

Board-Denied Claims

After the Board has denied a petition that also constitutes a claim for refund, and the assessee has paid the tax, the action must be filed within four years of:

- The mailing of the Board's written decision on the petition; or

- The mailing date of the Board's written findings and conclusion on the petition, whichever is later.

County-Denied Claims

The action must be filed within six months from the date of the county board of supervisors' notice of action on the claim. If the county does not send a decision notice within six months of the date the claim is filed, the assessee may consider the claim denied and file an action in superior court.

AUDIT REVIEW AND ESCAPE ASSESSMENTS

AUDIT CONFERENCE

The Board periodically audits the records of state assessees to review information relating to the value of their property. If a disagreement over an audit conclusion arises during an audit, an assessee may attempt to resolve the dispute through discussion with the Board auditor and/or through the provision of more information in support of the assessee's position.

After the audit, Valuation Division staff mail a copy of the preliminary audit report, and, if requested, copies of the audit work papers to the assessee. If the assessee disagrees with the conclusions of the report, he or she may request a meeting with the auditor and the auditor's supervisor. If, after discussion, the Board auditor is persuaded that any aspect of the audit is incorrect, he or she may revise the audit findings accordingly.

Following the meeting with the auditor and the auditor's supervisor, the Board mails the assessee a revised audit report setting forth any unresolved matters. Accompanying the revised report is a notice advising that the assessee has 30 days in which to present any new information or evidence to support the assessee's position.

ESCAPE ASSESSMENT APPEALS

If the audit findings indicate that any property has escaped assessment or been underassessed, the Board's Valuation Division staff will recommend to the Board that an "escape assessment" for the property should be made. If the Board approves the escape assessment, at least 30 days prior to transmitting a statement of assessment of the escaped property, a "Notice of Escape Assessment" describing the escape assessment and advising of appeal rights is sent to the assessee. The process for appealing an escape assessment and filing a claim for refund is the same as that followed for contesting other Board assessments, as previously discussed.

SUMMARY OF APPEALS ACTIVITIES AND PERTINENT DATES AND/OR DEADLINES

Valuation Process

Action (by taxpayer, unless noted)	Date/deadline
File property statement	by March 1
Board holds public hearings	February and May
Board issues notice of value —Unitary properties	by June 1
Board issues notice of value — Nonunitary properties	by last day of July
Assessment becomes final	July 20 for unitary property if a timely petition for reassessment is not filed with the Board. September 20 for nonunitary property if a timely petition for reassessment is not filed with the Board.

Appeals of Assessments and Related Penalties

Action (by taxpayer, unless noted)	Date/deadline
Request copy of staff capitalization studies/calculations	
File petition for reassessment of unitary property	petition for reassessment of unitary property to be filed no later than July 20 of the year of the assessment notice
File petition for reassessment of nonunitary property	petition for reassessment of nonunitary property to be filed no later than September 20 of the year of the assessment notice
File claim for refund	with original petition, or with county within four years of payment of the tax
Board hearing and decision	by December 31 of the year in which the assessment is made
File action in superior court	after Board denial of a petition and claim for refund, within four years of the mailing date of the Board's written decision on the petition or the mailing date of the Board's written findings and conclusion on the petition, whichever is later; or within 6 months after denial of a timely filed claim for refund or if after 6 months the board of supervisors has not taken action on claim for refund, an action may be filed at any time

Appeal of Allocated Assessment

Action (by taxpayer, unless noted)	Date/deadline
File petition for correction with Board	petition for correction may be filed no later than July 20 of the year of that notice
File claim for refund	with original petition, or with county within four years of payment of tax
Board hearing and decision	as specified in hearing notice, but by December 31 of the year in which the assessment is made
File action in superior court	after Board denial of a petition and claim for refund, within four years of the mailing date of the Board's written decision on the petition or the mailing date of the Board's written findings and conclusion on the petition, whichever is later; or within 6 months after denial of a timely filed claim for refund or if after 6 months the board of supervisors has not taken action on claim for refund, an action may be filed at any time

Contesting the Results of an Audit

Action (by taxpayer, unless noted)	Date/deadline
Let auditor know you disagree with conclusions	anytime during audit
Send letter detailing objections to auditor's supervisor	
Meet with auditor and auditor's supervisor	
Board sends revised audit report	
Submit new evidence	30 days, as specified in audit report
Board adopts and notices escape assessment for underassessed property	
File petition appealing escape assessment	(See "Appeals of Assessments and Related Penalties")

APPENDIX A: PRIVATE RAILROAD CAR TAX

The assessment of private railroad cars (PRRCs) differs from that of other public utility property, including railroad property, in significant respects. First, because of their mobility, most PRRCs are physically situated in California for only a portion of the year, and therefore must be assessed on a basis that considers this changing tax situs. Second, unlike other state assessed property, the Board not only assesses PRRCs but also levies and collects the corresponding property tax, with the resulting tax revenues going to the state's General Fund rather than local government. This appendix reviews the statutory basis for the Board's assessment of PRRCs, presents the method of assessment prescribed by law, and describes the Board's other duties relating to the Private Railroad Car Tax.

STATUTORY BASIS

Section 19 of article XIII provides the requirement that the Board assess private railroad car companies. Sections 11201 through 11702 of the Revenue and Taxation Code provide for the taxation of private railroad cars, prescribe the method of assessment, and generally define the Board's duties in regard to the Private Railroad Car Tax. Specifically, section 11251 provides that, "Private railroad cars operated upon railroads into, out of, or through this state shall be assessed and taxed by the board as prescribed in this part."

Section 11203 defines the private railroad cars subject to the tax. In general, these include any railroad rolling stock that is operated on railroads within the state, owned by an entity other than a railroad or the National Railroad Passenger Corporation, and intended to transport people, commodities, or materials.[42]

Railroad cars owned or leased by railroads are assessed as part of the railroad, as discussed earlier in this manual. Cars owned by the National Railroad Passenger Corporation (Amtrak) or the federal government are exempt from property taxation.

Individual persons or companies that are not rail car companies may own passenger cars and pay the railroads fees to transport the cars. These are commonly known as "palace cars." Such cars

[42] Certain railroad cars are specifically excluded from the tax. Section 11203 provides:
"(b) 'Private railroad car' does not include: (1) Freight train or passenger train cars owned by railroad companies which are used or subject to use under the ordinary per diem agreement common to all railroads. (2) Freight train or passenger cars handled under mileage or through line contract arrangements between railroad companies. (3) Cars owned by or leased to any railroad company operating in this state, or by any railroad company operated as part of the same railroad system as the company operating in this state, and used by the railroad company in the operation, maintenance, construction, or reconstruction of its property and assessed and taxed in this state as a part of the property of a railroad company operating in this state. (4) Passenger train cars, other than those described in subdivision (b), that are privately owned and for which the owner pays the railroad a fee, regardless of how calculated, for transporting such cars. (5) Any railroad rolling stock for which a railroad or the National Railroad Passenger Corporation is the lessee. For a leased car, the car's Association of American Railroad's, or successor organization's reporting mark is rebuttably presumed to be the mark of the lessee."

are not subject to state assessment; they are subject to local assessment to the extent they have tax situs in a county.

The Private Railroad Car Tax applies only to *rail cars*, not to tools, shop equipment, materials, any personal property typically used or kept at fixed locations to repair, improve, service, or operate the cars, or to any other railroad property.

ASSESSMENT

Rail cars often begin their route from a "terminal" state and travel through many "bridge" states before completing their trip in another terminal state. The cars deliver their cargo in a terminal state and typically remain there for a period of time while waiting for another load.

California law prescribes the car-day method of assessment. As described in section 11293, under this method, the average number of each class of rail car physically present in California in the calendar year preceding the fiscal year of the assessment is multiplied by the value of a rail car of that class to determine the assessment.

Railroad companies with interstate operations involving California measure rail car movement into and out of California and report this information to the Board, using car-type codes originally established by the Association of American Railroads and prescribed in section 11292. Board staff analyze this data to determine the number of days each class of car is in California.[43] The results are converted to an equivalent number of cars for each class of car; in other words, car-days are converted to car-years. The time that cars are not "qualified for revenue service," subject to specified limitations, is excluded from the number of car days in California.[44]

For example, if a company's class T cars (i.e., tank cars) were in California a total of 750 days, and the cars were not qualified for revenue service for 20 days, the equivalent number of cars of that class in California for the entire year is 2.0 ([750 days – 20 days]/365 days).

The estimated value of a rail car is based on its acquisition cost less depreciation, as prescribed in section 11292. Briefly, depreciation is calculated on a straight-line basis with a maximum of 80 percent depreciation allowed. Stack cars (class S), lightweight, low profile intermodal (class Q), flat cars (class F), conventional intermodal (class P), and vehicular flat (class V) use 22 years minus the age at acquisition for depreciable life. All other cars use 25 years minus the age at acquisition for depreciable life.

To determine the assessment, or taxable value, the equivalent number of cars in California for each class of car is multiplied by the estimated value for each class of car.

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[43] Section 11316 provides for a 10 percent penalty of the value of the estimated or escaped assessment for any escape due to taxpayer negligence and a penalty of 25 percent of the value of the estimated or escaped assessment for any fraudulent or willful attempt to evade tax by the taxpayer.

[44] See section 11294.

LEVY AND COLLECTION OF TAX

As noted at the outset, the Board not only assesses private railroad cars but also levies and collects the corresponding property taxes. Under section 11401, the Board must levy a tax on private railroad cars on or before October 1 of each year. Under section 11404, on or before October 15 of each year, the Board must mail out a notice stating the amount of assessment, the rate and amount of tax, and a demand for payment of the tax to the Board no later than the following December 10.[45] As stated in section 11401, the Board calculates the tax rate for private railroad car assessments as the "next preceding year's" average rate of general property taxation in the state.[46]

DISPOSITION OF TAX PROCEEDS

Section 11701 prescribes that all revenues collected by the Board from the Private Railroad Car Tax be transmitted to the State Treasurer for deposit to the state treasury and credit to the state's General Fund.[47] As noted earlier, property taxes resulting from all other state assessments are levied and collected at the local level and are used to support local government.

[45] Section 11405 provides for a penalty of 10 percent of the tax plus interest on the amount of the tax at the adjusted rate pursuant to section 19521, from December 10 until the date of payment.

[46] The computation of the tax rate is prescribed in section 11403, which states: "The board shall compute the average rate of general property taxation in the state by: (a) Adding the county, city, school district, and other general taxes, but not the special taxes on intangibles, aircraft, baled cotton or any other property which is subject to a uniform statewide tax rate, nor special assessments, and (b) Dividing the amount obtained by the total assessed valuation in the state as shown by the county tax rolls for the same year. 'Total assessed valuation' as used in this section, does not include the assessments of property which is subject to a uniform statewide tax rate. 'Special assessments,' as used in this section, mean any amount levied solely against real estate or real estate and improvements."

[47] Pursuant to section 11702, upon warrant by the Controller, these monies shall be appropriated for any refunds that may be necessary.

APPENDIX B: PROPERTY TRANSACTIONS AND JURISDICTIONAL CHANGES

Various types of property transactions involving state and local assessees may produce changes in assessment jurisdiction—that is, from state assessed to locally assessed, or vice versa. This appendix discusses jurisdiction in light of several typical property transactions.

GENERAL CONCEPTS

Several general concepts relating to jurisdiction constitute the background for resolving jurisdictional issues in specific situations. Many of these concepts were also discussed in Chapter 1.

(1) The Board's assessment jurisdiction is prescribed in section 19 of article XIII of the California Constitution:

> The Board shall annually assess (1) pipelines, flumes, canals, ditches, and aqueducts lying within 2 or more counties and (2) property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the State, and companies transmitting or selling gas or electricity….

Constitutional mandate thus establishes two jurisdictional criteria: (1) a criterion based on the type of property and (2) a criterion based on the type of company.

The criterion based on type of property includes all property necessary for the operation of intercounty pipeline, flumes, canals, ditches and aqueducts. Excluded from property meeting this criterion, however, are interests in land, ancillary delivery facilities, and personal property not directly related to the proper mechanical functioning of a pipeline, flume, canal, ditch, or aqueduct.

The criteria based on type of company includes all property owned or used by regulated railway, telegraph or telephone companies; rail car companies and companies that sell or transmit gas or electricity.

All taxable property that is not subject to state assessment by the Board is subject to local assessment by county assessors.

(2) Property subject to state assessment includes property that is *owned or used* by the state assessee. Thus, all property leased by a state assessee is subject to state assessment regardless of the lease term.

(3) While, there is no constitutional provision allowing the Board to delegate the assessment of property *owned* by a state assessee to local assessors, the Board may delegate the assessment of certain property *used* by state assessees. As stated in section 19 of article XIII:

> … The Board may delegate to a local assessor the duty to assess a property *used but not owned* by a State assessee on which the taxes are to be paid by a local assessee. [Emphasis added.]

Thus, the Board may delegate the duty to assess property leased by a state assessee to the local assessor if a local assessee owns the property and the local assessee-owner pays the property taxes. For example, on March 29, 2001, the Board of Equalization decided to delegate the duty to assess leased wireless communication tower sites to county assessors whenever constitutionally permissible.[48] As a result, wireless communication tower sites that are used but not owned by state assessees, on which the property taxes are paid by a local assessee, have been delegated to county assessors. The Board's decision was effective with the January 1, 2001, lien date.

There is a qualification that involves leasehold improvements, however. When delegating assessment duty, the Board retains assessment jurisdiction over fixtures installed by the state assessee. The assessment of structural items is typically delegated to the local assessor together with the land and all other improvements.

(4) Since locally assessed property generally is assessed under the provisions of article XIII A of the California Constitution while state assessed property is not, when the assessment jurisdiction of a property changes, the method of assessment also changes. For example, if a state assessed property becomes locally assessed, it should be assessed as all other locally assessed property, and vice versa.

(5) Generally, property transactions between a state assessee and another state assessee or between a local assessee and another local assessee have no effect on assessment jurisdiction. For example, if one state assessee sells property to another state assessee, generally no assessment action is required by the local assessor.

SOME TYPICAL SITUATIONS

SALE OR LEASE OF PROPERTY FROM LOCAL ASSESSEE TO STATE ASSESSEE

Property purchased or leased by a state assessee from a local assessee is subject to Board assessment jurisdiction as of the date of transfer. Although the Board may, in certain circumstances, delegate assessment jurisdiction of a leasehold improvement to the county assessor, the assessor should notify the Board of the transfer and remove the property from the local assessment roll on the following lien date. During the period the property remains on the local roll, it is assessed in accordance with article XIII A. If the property is inadvertently double assessed, taxes on all or any portion of an assessment of state assessed property may be cancelled, pursuant to section 5011.

[48] Letter To Assessors 2001/024, *Delegation of Assessment Jurisdiction of Wireless Communication Tower Sites*.

The Board will assess the property on the following lien date, in accordance with subdivision (b) of section 722.5:

> … real property that becomes subject to board assessment on or after January 1, and on or before the following January 1, shall not be state assessed until the assessment year commencing on the latter January 1.

Even though the property will not be assessed by the Board until the following January 1, it comes under state jurisdiction on the date of the change in ownership. After the property becomes subject to state assessment, the county assessor has no authority to make any new assessment regarding the property. Thus, neither the change in ownership itself nor any subsequent new construction (i.e., new construction that occurs between the date of transfer and the following lien date) is subject to supplemental assessment by the county assessor. Section 75.14 states in part "A supplemental assessment pursuant to this chapter shall not be made for any property not subject to the assessment limitations of Article XIII A of the California Constitution." Since a new base year value under article XIII A is not established on property transferred to a state assessee, no supplemental assessment can occur.

A question may also arise regarding assessment appeals jurisdiction. If an assessee files an appeal during the period after a locally assessed property becomes subject to state assessment but before the property is assessed on the Board roll, the issue on appeal would relate to the prior assessment. Since that assessment was made on the local roll at a time when the property was subject to local assessment, the local appeals board would have jurisdiction. Contrariwise, if the issue on appeal relates to an assessment made on the Board roll after the property became subject to state assessment, the Board of Equalization would have appeals jurisdiction.

SALE OF PROPERTY FROM STATE ASSESSEE TO LOCAL ASSESSEE

Property purchased by a local assessee from a state assessee is subject to local assessment jurisdiction, and therefore subject to the provisions of article XIII A, as of the date of change in ownership. The property is subject to supplemental assessment by the county assessor. Subdivision (a) of section 722.5 contains specific reference to supplemental assessment provisions (sections 75 and following):

> Real property assessed by the board … which thereafter becomes subject to local assessment, shall not be assessed locally during the remainder of the assessment year, except as provided in Chapter 3.5 (commencing with Section 75) of Part 0.5 of Division 1.

The amount of the supplemental assessment is the difference between the property's new base year value as established by the county assessor and the taxable value on the current Board roll. The taxable value on the current Board roll is the portion of the state assessed value allocable to the subject property. As stated in section 75.9:

> … In the case of real property which, prior to the date of the change in ownership or completion of new construction, was assessed by the board pursuant to section

19 of article XIII of the California Constitution, "taxable value" means that portion of the state-assessed value determined by the board to be properly allocable to the property which is subject to the supplemental assessment.

Contact between the county and the Board's Valuation Division is necessary to determine the allocated value.

SALE AND LEASEBACK BY STATE ASSESSEE

In a typical sale-leaseback transaction, the sale and leaseback are essentially simultaneous. In a sale-leaseback involving a state assessee, the state assessee owner-seller, immediately becomes the lessee. There is generally no change in assessment jurisdiction, since all property owned or *used* (i.e., leased) by a state assessee is subject to state assessment. The property remains state assessed even though the state assessee is merely leasing it, unless the agreement specifies that not all of the property is leased to the state assessee, and the purchaser/lessor is to pay the property taxes. Article XIII section 19 states that "the Board may delegate to a local assessor the duty to assess a property used but not owned by a state assessee on which the taxes are to be paid by the local assessee."

PROPERTY OWNED BY LOCAL ASSESSEE AND LEASED TO STATE ASSESSEE WITH SALE OF LESSOR'S INTEREST

Generally, a change in ownership of the underlying fee interest (i.e., the lessor's interest) in a local assessee-owned but state assessed property (i.e., the property is leased to a state assessee) does not change the assessment jurisdiction. Since the property remains leased to a state assessee, it remains under Board jurisdiction.

No action should be taken by the county assessor. This is true even if the remaining term of the lease is less than 35 years; in which case, if the property were under local assessment jurisdiction, there would be a change in ownership. However, because the property remains under state assessment jurisdiction, it is not subject to the change in ownership provisions of article XIII A.

Since the Board may delegate to the assessor the duty to assess property that is "used" but not "owned" by a state assessee and on which the taxes are paid by the local assessee, such delegation generally occurs for buildings and leasehold improvements that are "partially" leased and/or occupied by state assessees. The Board may not, however, delegate the assessment of any portion of a state assessee's improvements, including leasehold improvements, if they are "owned" by the state assessee.

PROPERTY OWNED BY A LOCAL ASSESSEE AND LEASED TO STATE ASSESSEE WITH LEASE TERMINATION

In this scenario, assessment jurisdiction changes from state to local as of the date of lease termination because after that point in time a state assessee neither owns nor uses the property. As locally assessed, the property becomes subject to article XIII A.

If the lease was for an original term of 35 years or more, the termination of the lease is a change in ownership, and the county assessor should reassess the property and establish a new base year value. The assessor should also issue a supplemental assessment. Since the property is owned by a local assessee, the property was previously assessed on the local roll and hence a base year value for the property should exist. The base year value of the property should be revised, if necessary, to reflect any incremental base year value(s) resulting from new construction while the property was subject to state assessment. If the improvement was constructed and immediately occupied by the state assessee—for example, under a ground lease arrangement—a base year value for the improvement will not exist. The assessor should determine what the base year value of the improvements would have been as of the date of their completion.

If the lease was for an original term of less that 35 years, then there is no change in ownership and hence no reassessment or supplemental assessment. For the lien date following lease termination, the county assessor should enroll a taxable value consistent with the provisions of article XIII A. Normally, this would be the lesser of the property's factored base year value or current market value, as prescribed in subdivision (a) of section 51.

FOREIGN IMPROVEMENTS

Improvements owned by one party and located on land owned by another party are called "foreign improvements." For example, leasehold improvements owned by a lessee/tenant are a type of foreign improvement. Foreign improvements owned by a local assessee on state assessed land are subject to local assessment if the improvements are not used by (i.e., leased by) the state assessee. The county assessor should assess such improvements as he or she assesses other locally assessed property. In the case of foreign improvements owned by a state assessee on land owned by a local assessee, both the improvements and the land are state assessed—the improvements because they are owned by the state assessee and the land because it is used by the state assessee.

When a state assessee leases property owned by a local assessee, and the taxes are paid by the local assessee, the Board may delegate its authority to assess the building or structure to the county assessor. As discussed above, however, the assessment of leasehold improvements owned by a state assessee located in or on such a building or structure may not be delegated. Under article XIII, section 19, the Board retains its authority to assess leasehold improvements owned by a state assessee, and such improvements should not be assessed by the county assessor.

LESSOR'S EXEMPTION CLAIMS

If a lessor's exemption is sought for state assessed property, the property owner must file a lessor's exemption claim form with the local assessor where the property is located. The Board has no authority to grant the exemption; this power rests with county assessors. The assessor receiving an exemption claim involving state assessed property should act on the claim in the same manner as a claim for locally assessed property. After the claim is processed, the assessor should forward a copy of the claim form with advice of the assessor's determination to the Board's Valuation Division.

DISCOVERY OF STATE ASSESSED PROPERTY

The Board's discovery of state assessed property is largely through taxpayer reporting. A state assessee is required to file an annual property statement detailing, among other things, all property owned or used, except licensed motor vehicles, as of the lien date.

County assessors' offices may discover property under state jurisdiction as part of their normal assessment duties (e.g., the processing of changes in ownership, memoranda of leases, and building permits). When an assessor discovers that a state assessee has purchased or leased locally assessed property, the assessor should notify the Board's Valuation Division. If the Board determines that it has assessment jurisdiction, the Valuation Division will notify the local assessor via a "List of Land Changes." The Board will also send new land identification maps to the assessor identifying the property with a Board (SBE) parcel number.

In order to determine the assessment jurisdiction for newly constructed improvements, assessors should send copies of all building permits relating to construction by state assessees or their contractors to the Valuation Division. If Valuation Division staff determines that the newly constructed improvements authorized by a particular permit are not subject to state assessment, the assessor will be notified by staff to locally assess the property.

STATE BOARD OF EQUALIZATION MAPS AND PARCEL NUMBERS

The Board sends land identification maps (Board maps) to local assessors when there is a change in assessment jurisdiction. The maps describe the property involved with respect to officially established survey lines, corners, or other reference points shown on maps of record. The Board's parcel numbers (SBE parcel numbers) are quite different from the parcel numbers (APNs) assigned by local assessors. The numbers derive from completely distinct mapping systems.

Each parcel of land owned or used by a state assessee is assigned a unique parcel number. Each SBE parcel number has four groups of characters—for example, 872-27-16D-1A.

1. The first group of characters is a unique number assigned to each state assessee. In this example, "872" represents Southern Pacific Railroad Company. Assessees are numerically grouped by industry as follows:

Industry	*SBE Number*		
Gas, Electric, Water and Gas Transmission	100	—	199
Local Exchange Telephone Companies	200	—	399
Pipeline Companies	400	—	499
Railcar Maintenance Facilities	500	—	699
Railroad Companies	800	—	899
Electric Generation Companies	1100	—	1199
Long Distance Telephone Companies	2000	—	2499
Wireless Telephone Companies	2500	—	2599
Radio Common Carrier Companies	3000	—	3999
Long Distance Telephone Companies	7500	—	7999
Wireless Telephone Companies	D001	—	D999
Long Distance Telephone Companies	P001	—	~~P999~~Q999

2. The second group of characters is a unique code for each county. In the example, "27" represents Monterey County. County numbers are as follows:

County Number	*County Name*	*County Number*	*County Name*
1	Alameda	30	Orange
2	Alpine	31	Placer
3	Amador	32	Plumas
4	Butte	33	Riverside
5	Calaveras	34	Sacramento
6	Colusa	35	San Benito
7	Contra Costa	36	San Bernardino
8	Del Norte	37	San Diego
9	El Dorado	38	San Francisco
10	Fresno	39	San Joaquin
11	Glenn	40	San Luis Obispo
12	Humboldt	41	San Mateo
13	Imperial	42	Santa Barbara
14	Inyo	43	Santa Clara
15	Kern	44	Santa Cruz
16	Kings	45	Shasta
17	Lake	46	Sierra
18	Lassen	47	Siskiyou
19	Los Angeles	48	Solano
20	Madera	49	Sonoma
21	Marin	50	Stanislaus
22	Mariposa	51	Sutter
23	Mendocino	52	Tehama
24	Merced	53	Trinity
25	Modoc	54	Tulare
26	Mono	55	Tuolumne
27	Monterey	56	Ventura
28	Napa	57	Yolo
29	Nevada	58	Yuba

3. The third group of characters identifies the map and its position in a series. This group consists of from 1 to 3 characters. In the example, "16" indicates that the map is the 16th in a series of maps for that county. Each map change from the original map filed is noted by an alphabetical suffix, "A," "B," "C," etc. In the example, "16A" indicates that this map is a supplementary map that has been filed. With each map revision the specific parcels will be renumbered starting from 1.

4. The fourth part of a SBE parcel number identifies a specific parcel. This group consists of from 1 to 3 characters. A change to a specific parcel is noted by an alphabetical suffix. In the example, "1A" indicates that it has been revised once.

State assessed property that transfers from one state assessee to another does not receive a new SBE parcel number. Instead, SBE parcel numbers are listed following the new owner's company number. For example, the state assessee number for Union Pacific Railroad Company that is "843." If the example property were acquired by Union Pacific Railroad Company, the property would simply be listed under 843, and the new SBE parcel number would be 843-872-27-16D-1A.

-APPENDIX C: BOARD PROPERTY CLASSIFICATION CODES

The Board classifies property reported by an assessee by classification code. The following tables contain the classification codes for various types of unitary and nonunitary property.

Unitary

Code	*Description*
001	Operating Property – Land
002	Operating Property – Improvements
003	Operating Property – Personal Property
011	Possessory Interest – Land
012	Possessory Interest – Improvements
021	Miscellaneous Other Rights – Land
022	Miscellaneous Other Rights – Improvements
023	Miscellaneous Other Rights - Personal Property
041	Leased Land
042	Leased Improvements
043	Leased Personal Property
071	Property Which is to Show Separately on the Roll for any Reason Except as Indicated Above – Land
072	Property Which is to Show Separately on the Roll for any Reason Except as Indicated Above – Improvements
073	Property Which is to Show Separately on the Roll for any Reason Except as Indicated Above – Personal Property
083	Aircraft
101	Hannigan Unitary Land (not 000-001)
102	Hannigan Unitary Improvements (not 000-001)
103	Hannigan Unitary Personal Property (not 000-001)
221	Fiberoptic R/W
401	Unitary Timber Preserve Zone Land
421	Gas Transmission R/W

Nonunitary

Code	*Description*
~~051~~	~~Leased Property to be Assessed to Non-utility Owner - Land~~
~~052~~	~~Leased Property to be Assessed to Non-utility Owner - Improvements~~
~~053~~	~~Leased Property to be Assessed to Non-utility Owner - Personal Property~~
061	Property Exempt From Taxation Under Section 3 of Article XIII of the Constitution - Land
062	Property Exempt From Taxation Under Section 3 of Article XIII of the Constitution - Improvements
091	Non-operating – Land
092	Non-operating – Improvements
093	Non-operating – Personal Property
191	Operating Nonunitary – Land
192	Operating Nonunitary – Improvements
193	Operating Nonunitary - Personal Property
491	Nonunitary Timber Preserve Zone Land
891	Nonunitary Railroad Transportation Property – Land
892	Nonunitary Railroad Transportation Property – Improvements
893	Nonunitary Railroad Transportation Property – Personal Property

Property Classification Summary Table

Property Group	*Land*	*Imps*	*PP*
Operating Property	001	002	003
Possessory Interest	011	012	
Miscellaneous Other Rights	021	022	023
Leased	041	042	043
Exempt Property	061	062	
Aircraft			083
Property Shown Separately on the Roll	071	072	073
Non-operating Nonunitary	091	092	093
Hannigan Unitary Property	101	102	103
Operating Nonunitary	191	192	193
Fiber Optic Right of way	221		
Unitary TPZ Land	401		
Gas Transmission Right of Way	421		
Nonunitary TPZ Land	491		
Nonunitary Rail Transportation Property	891	892	893

APPENDIX D: STATE ASSESSMENT CALENDAR

Date	*Party*	*Activity*	*Authority*
January 1	State assessees	State assessed property shall be assessed at its fair market or full value as of 12:01 a.m. on the first day of January.	§ 722 Rev. & Tax. Code
No later than January 30	Executive Director	The Executive Director shall provide the Board with a proposed schedule of dates that will govern the actions to be taken pursuant to Rule 902 (*Unitary Property Value Indicators and Staff Discussions*), Rule 903 (*Discussion with Board of Unitary Property Value Indicators*), and Rule 904 (*Unitary and Nonunitary Property Value Determinations and Petitions for Reassessment*), no later than November 30 each year. Upon Board approval, but no later than January 30 of the next year, the Executive Director shall inform all state assessees of the schedule adopted by the Board.	Rule 901.5 Property Tax Rules
Between the first day of January and the first day of June	Board	The Board shall mail notice to the assessee stating the amount of the assessed value of the assessee's unitary property. The Board shall also advise the assessee that a petition for reassessment of the nonunitary property may be filed no later than July 20 of the same calendar year in which the notice is provided. The Board may extend the petition-filing period once for a period not to exceed 15 days, provided a written request for the extension is filed prior to the expiration of the period for which the extension may be granted.	§ 731 & § 733 Rev. & Tax. Code
Between the first day of January and the last day of July	Board	The Board shall mail notice to the assessee stating the amount of the assessed value of the assessee's nonunitary property. The Board shall also advise the assessee that a petition for reassessment of the nonunitary property may be filed no later than September 20 of the same calendar year in which the notice is provided. The Board may extend petition-filing once for a period not to exceed 15 days, provided a written request for the extension is filed prior to the expiration of the period for which the extension may be granted.	§ 732 & § 733 Rev. & Tax. Code
March 1	State assessees	Last day to file property statements with the Board for requests mailed on or before January 1. Assessees have 60 days from mailing date of requests mailed after January 1 to file property statements. Rule 901 provides that the Board may grant an extension for cause not to exceed 30 days.	§ 830 & § 830.1 Rev. & Tax. Code Rule 901 Property Tax Rules
On or before April 30	Private railroad cars	The annual report required by § 11271 of the Revenue and Taxation Code of all persons whose private railroad cars operated upon the railroads of this state at any time during the prior calendar year shall be filed on or before April 30.	§ 11271 Rev. & Tax. Code Rule 1001 Property Tax Rules
May 30	Any subscriber to the Board's tax-rate area change service	Any subscriber to the Board's tax-rate area change service and who receives a change mailed between April 1 and May 1, shall file a corrected statement no later than May 30. If change mailed after May 1, a corrected statement shall be filed no later than the 60th day following the mailing of change.	§ 830(d) Rev. & Tax. Code

Date	*Party*	*Activity*	*Authority*
No later than May 31	Board	The Board will make and publicly announce individual unitary-value determinations no later than May 31. The Chief of the Valuation Division shall notify the state assessees of the values determined by the Board. A copy of an appraisal data sheet containing the staff value indicators and value recommendations to the Board shall accompany the notice.	Rule 904(a) Property Tax Rules
On or before the last day of June	Chief, Valuation Division	The Chief of the Valuation Division of the State Board of Equalization shall notify the state assessees of the values of nonunitary property.	Rule 904(b) Property Tax Rules
No later than June 15	Board	Board shall notify the proposed allocation of assessed unitary values to the assessees. Notice will also inform state assessees that they may file a petition for a correction of an allocated assessment no later than July 20 of the same calendar year in which the notice is provided.	§ 746 Rev. & Tax. Code
On or before the last day of June	Chief, Valuation Division	The Chief of the Valuation Division of the State Board of Equalization shall notify state assessees of the allocated assessed unitary values of each assessee.	Rule 904(c) Property Tax Rules
On or before July 15	Board	Board shall transmit estimates of total assessed values of state assessed property to county auditors.	§ 755 Rev. & Tax. Code
Prior to July 31	Board	Notify petitioners of its decisions on petitions for corrections of allocated assessments.	§ 749 Rev. & Tax. Code
On or before July 31	Board	Transmit changes to estimates of total assessed values of state assessed property to county auditor.	§ 755 Rev. & Tax. Code
On or before July 31	Board	• Board adopts assessment rolls. • Staff transmits assessment rolls to county auditors. • Roll is open to inspection by interested agencies and districts.	§ 756 Rev. & Tax. Code
On or before December 31	Board	Notify petitioners of its decisions on petitions for corrections of allocated assessments.	§ 749 Rev. & Tax. Code
December 31	Board	Last day to complete decisions on petitions for reassessment of unitary and nonunitary values.	§ 744 Rev. & Tax. Code

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APPENDIX E: CONSTITUTIONAL PROVISIONS, STATUTES, REGULATIONS, AND SIGNIFICANT CASES[49]

CONSTITUTIONAL PROVISIONS

Article XIII, Section 14

Property to be assessed where situated. All property taxed by local government shall be assessed in the county, city, and district in which it is situated.

Article XIII, Section 19

State board to assess and tax property of public utilities. The Board shall annually assess (1) pipelines, flumes, canals, ditches, and aqueducts lying within 2 or more counties and (2) property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the State, and companies transmitting or selling gas or electricity. This property shall be subject to taxation to the same extent and in the same manner as other property.

No other tax or license charge may be imposed on these companies which differs from that imposed on mercantile, manufacturing, and other business corporations. This restriction does not release a utility company from payments agreed on or required by law for a special privilege or franchise granted by a government body.

The Legislature may authorize Board assessment of property owned or used by other public utilities.

The Board may delegate to a local assessor the duty to assess a property used but not owned by a state assessee on which the taxes are to be paid by a local assessee.

STATUTES

REVENUE AND TAXATION CODE PROVISIONS

Section 100

Unitary and operating nonunitary property. Notwithstanding any other provision of law, commencing with the 1988–89 fiscal year, property tax assessed value attributable to unitary and operating nonunitary property, as defined in Sections 723 and 723.1, that is assessed by the State Board of Equalization shall be allocated by county as provided in Section 756, and the assessed value and revenues attributable to that allocation shall be allocated within each county as follows:

[49] The information in this appendix was current as of the publication date. The information may not reflect current law.

(a) Each county shall establish one countywide tax rate area. The assessed value of all unitary and operating nonunitary property shall be assigned to this tax rate area. No other property shall be assigned to this tax rate area.

(b) Property assigned to the tax rate area created by subdivision (a) shall be taxed at a rate equal to the sum of the following two rates:

(1) A rate determined by dividing the county's total ad valorem tax levies for the secured roll, including levies made pursuant to Section 96.8, for the prior year, exclusive of levies for debt service, by the county's total ad valorem secured roll assessed value for the prior year.

(2) A rate determined as follows:

(A) By dividing the county's total ad valorem tax levies for unitary and operating nonunitary property for the prior year debt service only by the county's total unitary and operating nonunitary assessed value for the prior year.

(B) Beginning with the 1989–90 fiscal year, adjusting the rate determined pursuant to subparagraph (A) by the percentage change between the two preceding fiscal years in the county's ad valorem debt service levy for the secured roll, not including unitary and operating nonunitary debt service.

(c) The property tax revenue derived from the assessed value assigned to the countywide tax rate area pursuant to subdivision (a) by the use of the tax rate determined in paragraph (1) of subdivision (b) shall be allocated as follows:

(1) For the 1988–89 fiscal year and each fiscal year thereafter, each taxing jurisdiction shall be allocated an amount of property tax revenue equal to 102 percent of the amount of the aggregate property tax revenue it received from all unitary and operating nonunitary property in the prior fiscal year, exclusive of revenue attributable to levies for debt service.

(2) If the amount of property tax revenue available for allocation in the current fiscal year is insufficient to make the allocations required by paragraph (1), the amount of revenue to be allocated to each taxing jurisdiction shall be prorated based on a factor determined by dividing the total amount of property tax revenue available to all taxing jurisdictions from unitary and operating nonunitary property in the current year, exclusive of revenue attributable to levies for debt service, by the total amount of property tax revenue received by all taxing jurisdictions from unitary and operating nonunitary property in the prior fiscal year, exclusive of revenue attributable to levies for debt service.

(3) If the amount of property tax revenue available for allocation to all taxing jurisdictions in the current fiscal year from unitary and operating nonunitary property, exclusive of revenue attributable to levies for debt service, exceeds 102 percent of the property tax revenue received by all taxing jurisdictions from all unitary and operating nonunitary property in the prior fiscal year, exclusive of revenue attributable to levies for debt service, the amount of revenue in excess of 102 percent shall be allocated to all taxing jurisdictions in the county by a ratio determined by

dividing each taxing jurisdiction's share of the county's total ad valorem tax levies for the secured roll for the prior year, exclusive of levies for debt service, by the county's total ad valorem tax levies for the secured roll for the prior year, exclusive of levies for debt service.

(d) The property tax revenue derived from the assessed value assigned to the countywide tax rate area pursuant to subdivision (a) by the use of the tax rate determined in paragraph (2) of subdivision (b) shall be allocated as follows:

(1) An amount shall be computed for each taxing jurisdiction and shall be determined by multiplying the amounts required in the current year pursuant to subdivisions (a) and (c) of Section 93 by that percentage that shall be determined by dividing the amount of property tax revenue the jurisdiction received in the prior year from unitary property and operating nonunitary property by the total amount of property tax revenue the jurisdiction received in the prior year from all property.

(2) The amount of property tax revenue available for allocation pursuant to this subdivision shall be allocated among taxing jurisdictions in the proportion that the amount computed for each taxing jurisdiction pursuant to paragraph (1) bears to the total amount computed pursuant to paragraph (1) for all taxing jurisdictions.

(3) If a taxing jurisdiction is levying a tax rate for debt service for the first time in the current fiscal year, for purposes of determining the percentage specified in paragraph (1), that percentage shall be the percentage determined by dividing the amount of property tax revenue received by that taxing jurisdiction in the prior year pursuant to subdivision (c) from unitary and operating nonunitary property by the total amount of property tax revenue received by that taxing jurisdiction in the prior year from all property within the taxing jurisdiction.

(e) For purposes of this section:

(1) "The county's total ad valorem tax levies for the secured roll" means all ad valorem tax levies for the county's secured roll, including the general tax levy, levies for debt service (including land only and land and improvement rates), and levies for redevelopment agencies.

(2) "The county's total ad valorem secured roll" means the county's local roll, after all exemptions except the homeowner's exemption, and the county's utility roll.

(3) "Taxing jurisdiction" includes a redevelopment agency.

(4) In a county of the second class, for the 1992–93 fiscal year and each fiscal year thereafter, "taxing jurisdiction" includes that fund that has been designated by the auditor as the "Unallocated Residual Public Utility Tax Fund." All revenues allocated to that fund pursuant to this section shall be deposited in that fund and shall be distributed as follows:

(A) For the 1992–93 fiscal year to the 1996–97 fiscal year, inclusive, at the discretion of the county board of supervisors.

(B) For the 1997–98 fiscal year, 100 percent to the Orange County Fire Authority.

(C) For the 1998–99 fiscal year and each fiscal year thereafter, in accordance with the following schedule:

(i) Fifty-seven and forty-seven hundredths percent to the Orange County Fire Authority.

(ii) Forty-one and forty-seven hundredths percent to the Orange County Library District.

(iii) Forty-eight hundredths percent to the Buena Park Library District.

(iv) Fifty-eight hundredths percent to the Placentia Library District.

(f) The assessed value of the unitary and operating nonunitary property shall be kept separate for each state assessee throughout the allocation process.

(g) Each state assessee shall be issued only one tax bill for all unitary and operating nonunitary property within the county.

(h) This section does not apply to unitary property of regulated railway companies.

(i) This section does not apply to property that on July 1, 1987, was undeveloped and owned by a utility and located within a city, county, or city and county that adopts a resolution stating that the property is subject to a development plan or agreement and that this section shall not apply to that property, and the city, county, or city and county transmits a copy of that resolution, including a legal description of the property, to the State Board of Equalization and the county's auditor-controller prior to January 1, 1988.

(j) (1) For property that on July 1, 1990, was undeveloped and owned by a utility and that is located within a city, county, or city and county that adopts a resolution stating that the property is subject to a development plan or agreement and that this subdivision applies to that property, and the city, county, or city and county transmits a copy of that resolution, including a legal description of the property, to the county auditor prior to August 1, 1991, the allocation of property tax revenues derived with respect to that property pursuant to Sections 96.1, 96.2, 97.31, 98, 98.01, and 98.04, shall be subject to the allocation required by paragraph (2).

(2) The county auditor shall annually allocate to a city, county, or city and county, that has adopted and transmitted a resolution pursuant to paragraph (1), the amount of property tax revenues derived with respect to the property described in paragraph (1) that would be allocated to that city, county, or city and county if that property were subject to assessment by the county assessor. In order to provide the allocations required by this paragraph, the county auditor shall make any necessary pro rata reductions in allocations to local agencies other than that city, county, or city and county adopting and transmitting a resolution pursuant to paragraph (1), of property tax revenues derived with respect to the property described in paragraph (1).

(k) (1) For property subject to this section that is owned by a utility that serves no more than two counties and is located within a city, county, or city and county that adopts a resolution stating

that the property is subject to a development plan or agreement for new construction and the city, county, or city and county transmits a copy of that resolution, including a legal description of the property, to the State Board of Equalization and the county auditor prior to January 1, 1995, the allocation of property tax revenues derived with respect to that property pursuant to Sections 96.1, 97.31, 98, 98.01, and 98.04, shall be subject to the requirements of paragraph (2) until December 31, 2004.

(2) If the city, county, or city and county has adopted and transmitted a resolution pursuant to paragraph (1), the county auditor shall annually allocate the property tax revenue attributable to the new construction described in the development plan or agreement, as if that new construction were subject to assessment by the county assessor, according to the following formula:

(A) An amount of property tax revenue to school entities, as defined in subdivision (f) of Section 95, equivalent to the same percentage the school entities received in the prior fiscal year of the property tax revenues paid by the utility in the county in which the property described in paragraph (1) is located.

(B) An amount of property tax revenue to the county in which the property is located equivalent to the same percentage the county received in the prior fiscal year of the property tax revenues paid by the utility in the county in which the property described in paragraph (1) is located. The county shall distribute those property tax revenues to the county general fund, the county library district, the county flood control district, the county sanitation districts, and the county service areas.

(C) The property tax revenue remaining after the allocations described in subparagraphs (A) and (B) are made shall be distributed to the city in which the property described in paragraph (1) is located.

(3) In order to provide the allocations required by paragraph (2), the county auditor shall make any necessary pro rata reductions in allocations of property taxes attributable to the property specified in paragraph (1) to jurisdictions other than those receiving an allocation under paragraph (2).

(4) The allocation required by this subdivision shall not apply to property tax revenues allocated on or after December 31, 2004.

Section 100.1

County allocations—railway companies. Notwithstanding any other provision of law, commencing with the 1988–89 fiscal year, property tax assessed value attributable to unitary property, as defined in Section 723, of a regulated railway company that is assessed by the State Board of Equalization, shall be allocated to tax rate areas as follows:

(a) Each tax rate area shall receive an amount of assessed value equal to the amount of assessed value received in the prior fiscal year adjusted for changes in track mileage unless the total amount of assessed value to be allocated is insufficient, in which case, each tax rate area shall

receive a pro rata share of the amount it received in the prior fiscal year adjusted for changes in track mileage.

(b) If the total amount of assessed value to be allocated is greater than the amount of assessed value allocated in the prior fiscal year adjusted for changes in track mileage, each tax rate area shall receive a pro rata share of the amount in excess of the prior year's assessed value of the regulated railway company adjusted for track mileage.

(c) If a tax rate area is divided, the prior fiscal year amount of assessed value of the unitary property of the regulated railway company shall be divided among the resulting tax rate areas in the same proportion that the track mileage on unitary property is divided among the resulting tax rate areas.

(d) The assessed value allocated to each tax rate area under subdivision (a), (b), or (c) shall be further allocated between land, improvements, and personal property in the same proportion as existed for each regulated railway company statewide in the 1987–88 assessment year.

(e) For purposes of this section:

(1) "The amount of assessed value received in the prior fiscal year adjusted for changes in track mileage" means the prior year's amount of assessed value in each tax rate area after it has been adjusted upward or downward in direct proportion to the change in the amount of track mileage on unitary property in the current year over the prior year.

(2) "Track mileage" means the number of miles of track adjusted to reflect the relative importance of mainline, branch, and other track.

Section 100.9

(a) Notwithstanding any other provision of law and except as provided in subdivision (b), for the 2003-04 fiscal year and each fiscal year thereafter, all of the following apply: (1) The property tax assessed value of an electric generation facility that is assessed by the State Board of Equalization shall be allocated entirely to the county in which the facility is located, and shall be allocated to that tax rate area in the county in which the property is located. (2) The tax rate applied to the assessed value allocated pursuant to paragraph (1) shall be the rate calculated pursuant to Section 93. (3) The revenues derived from the application of the tax rate to the assessed value allocated to a tax rate area pursuant to paragraph (1) shall be allocated among the jurisdictions in that tax rate area, in those same percentage shares that property tax revenues derived from locally assessed property are allocated to those jurisdictions in that tax rate area, subject to any allocation and payment of funds as provided in subdivision (b) of Section 33670 of the Health and Safety Code, and subject to any modifications or adjustments pursuant to Sections 99 and 99.2.

(b) Subdivision (a) does not apply to the assessed value or the revenues derived from that assessed value from either of the following: (1) An electric generation facility that was constructed pursuant to a certificate of public convenience and necessity issued by the California Public Utilities Commission to the company that presently owns the facility. (2) An electric

generation facility that is owned by a company that is a state assessee for reasons other than its ownership of the generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.

Section 108

"State assessed property." "State-assessed property" means all property required to be assessed by the Board under section 19 of article XIII of the Constitution and which is subject to local taxation.

Section 721

Valuation and assessment. The board shall annually value and assess all of the taxable property within the state that is to be assessed by it pursuant to section 19 of article XIII of the Constitution and any legislative authorization thereunder.

Section 721.5

(a) Notwithstanding Section 721 or any other provision of law to the contrary, commencing with the lien date for the 2003-04 fiscal year, the board shall annually assess every electric generation facility with a generating capacity of 50 megawatts or more that is owned or operated by an electrical corporation, as defined in subdivisions (a) and (b) of Section 218 of the Public Utilities Code. (2) For purposes of paragraph (1), "electric generation facility" does not include a qualifying small power production facility or a qualifying cogeneration facility within the meaning of Sections 201 and 210 of Title II of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. Secs. 796(17), (18) and 824a-3), and the regulations adopted for those sections under that act by the Federal Energy Regulatory Commission (18 C.F.R. 292.101-292.602).

(b) This section shall be construed to supersede any regulation, in existence as of the effective date of this section, that is contrary to this section.

Section 722

Ratio of assessed to full value. State-assessed property shall be assessed at its fair market value or full value as of 12:01 a.m. on the first day of January. The board shall annually prepare an assessment roll of the assessments made by it for transmittal to county auditors and city auditors as hereinafter provided in this chapter.

Section 722.5

Local and State assessment dates. (a) Real property assessed by the board pursuant to section 19 of article XIII of the California Constitution on January 1, which thereafter becomes subject to local assessment, shall not be assessed locally during the remainder of the assessment year, except as provided in Chapter 3.5 (commencing with Section 75) of Part 0.5 of Division 1.

(b) Personal property that becomes subject to Board assessment after January 1, and real property that becomes subject to board assessment on or after January 1, and on or before the following January 1, shall not be state assessed until the assessment year commencing on the latter January 1.

Section 723

Use of principle of unit valuation. The Board may use the principle of unit valuation in valuing properties of an assessee that are operated as a unit in a primary function of the assessee. When so valued, those properties are known as "unitary property." Property of an assessee not valued through the use of the principle of unit valuation are known as "nonunitary property." When valuing nonunitary property, the Board shall consider current market value information of comparable properties provided by the assessor just prior to the reappraisal by the Board of that property.

Section 723.1

Operating nonunitary properties. Operating nonunitary properties are those that the assessee and its regulatory agency consider to be operating as a unit, but the Board considers not part of the unit in the primary function of the assessee. This section does not apply to state-assessed property of regulated railway companies. In the case of regulated railway companies, there shall be only two classifications of property for purposes of this code, unitary and nonunitary.

Section 724

Timely performance. Whenever any act is required or allowed to be done on or before a date specified in this chapter and that day is a Saturday, Sunday or holiday, the act may be performed timely during the next following business day.

Section 725

Validity of assessment or taxes. The failure to receive any notice required to be given by the board or the failure of the Board to complete any action by a date specified under this chapter, shall not affect the validity of an assessment or the validity of any taxes levied pursuant thereto. When any notice given by the Board pursuant to this chapter provides for a time period of less than 10 days, the notice shall also be communicated by telephone on the day the notice is dated.

Section 731

Notification of assessment; unitary value. Each year between the first day of January and the first day of June, upon valuing the unitary property on an assessee, the Board shall mail to the assessee, at its address as shown in the records of the Board, a notice stating the amount of the assessed value of the assessee's unitary property. The notice shall advise the assessee that a petition for reassessment of the unitary property may be filed no later than July 20 of the same calendar year in which the notice is provided at the headquarters of the Board in Sacramento.

Section 732

Notification of assessment; nonunitary property. Each year between the first day of January and the last day of July, upon valuing the nonunitary property of an assessee, the Board shall mail to the assessee at its address shown in the records of the board a notice stating the amount of the assessed value of the assessee's nonunitary property. The notice shall advise the assessee that a petition for reassessment of the nonunitary property may be filed not later than September

20 of the same calendar year in which the notice is provided of the headquarters of the Board in Sacramento.

Section 733

Finality of assessment. (a) If a timely petition for reassessment is not filed with the Board, an assessment of unitary and nonunitary property of the assessee shall become final at the expiration of the period specified for filing a petition in the notice given in accordance with section 731 or section 732.

(b) The Board may extend the period for filing a petition for reassessment once for a period not to exceed 15 days, provided a written request for the extension is filed with the Board prior to the expiration of the period for which the extension may be granted.

Section 741

Petition for reassessment. A petition for reassessment of unitary or nonunitary property shall be in writing and shall state the specific grounds upon which it is claimed a correction or adjustment of the assessment is founded. The petition shall be delivered to the board at its headquarters office in Sacramento.

Section 742

Hearing on petition for reassessment. Upon receipt of a timely petition for reassessment, the Board shall set a time and place within the state for hearing on the petition. Notice thereof shall be mailed to the assessee at its address as shown in the records of the Board, not less than 10 working days in advance of the date of the hearing.

Section 743

Continuance of hearing; record; transcript. The hearing may be continued by the Board for good cause. The hearing shall be open to the public, except that upon conclusion of the taking of evidence the board may deliberate in private with the aid of its staff in reaching a conclusion. Upon written request, the board shall make a full record of the hearing and furnish the petitioner with a transcript thereof at the petitioner's expense.

Section 744

Notification of decision; findings and conclusions. (a) The Board shall notify the petitioner of its decision on a petition for reassessment by mail and shall make written findings and conclusions in requested at or prior to the commencement of the hearing. The Board shall send a periodic report of its decisions and any written findings and conclusions thereon to each county in which affected state-assessed property is situated. The findings shall fairly disclose the Board's determination of material factual issues and shall contain a statement of the method or methods of valuation used by the board in valuing the property. Notwithstanding the requirement for a statement of method or methods, the Board's approval of a settlement of a lawsuit contesting the value of state-assessed property shall be sufficient disclosure when value is

determined in accordance with a Board-approved settlement. Decisions of the Board on petitions for reassessment of state-assessed property shall be completed on or before December 31.

(b) When the value of an assessee's state-assessed property is determined, after a hearing on a petition for reassessment, to be different from the value originally adopted by the board, the board shall determine the year in which the corrected value is to be entered on the roll. The correct value may be entered on the roll for the fiscal in which the determination is made, or the difference between the original and the corrected value may be entered as an increase or decrease in the assessment for the succeeding fiscal year. If the corrected value is entered on the roll for the fiscal year in which it is determined, and the board roll has been transmitted to the county auditors, the Board shall make the corresponding changes in allocations and transmit the roll corrections to the county auditor.

(c) If the amount of the correction is to be entered on the roll for the succeeding fiscal year, an amount is to be added in lieu of interest. If the correction results in a reduction in assessed value, there shall be added to the reduction, in lieu of interest, 9 percent of the difference between the original assessed value, there shall be added to the increase, in lieu of interest, 9 percent of the difference between the original assessed value and the increased assessed value.

Section 745

Assessment; placement on roll. The assessment of the unitary and operating nonunitary property of an assessee shall be allocated to assessments on the roll prepared by the Board among the counties in which parts of the unitary and operating nonunitary property are situated. The assessment of the nonunitary property of an assessee shall be placed on the assessment roll prepared by the Board.

Section 746

Notification of proposed allocated assessed values of unitary property. Each year upon or prior to the completion of the assessment roll prepared by the board, but not later than June 15, the Board shall mail notice to each assessee at its address as shown on the records of the Board, of the allocated assessed values of the assessee's unitary property that have been or are proposed to be placed on the assessment roll to be transmitted to county auditors. The notice shall advise the assessee that a petition for a correction of an allocated assessment may be filed not later than July 20 of the same calendar year in which the notice is provided at the headquarters of the Board in Sacramento.

Section 747

Petition for correction of allocated assessment. A petition for correction of an allocated assessment shall be in writing and state the specific grounds upon which it is claimed a correction or adjustment in the allocation is founded. The value of the total unitary property of an assessee may not be brought into issue in a petition for correction of an allocated assessment.

Section 748

Hearing on petition for correction of allocated assessment. Upon receipt of a timely petition for correction of an allocated assessment, the board shall set a time and place within the state for a hearing on the petition. The Board shall mail notice of the time and place for the hearing to the assessee at its address as shown on the records of the Board not less than 10 working days prior to the date of the hearing.

Section 749

Record; transcript. Section 743 shall be applicable to hearings on petitions for correction of an allocated assessment and the Board shall notify the petitioner of its decision by mail. The decision shall include written findings and conclusions of the Board if requested at or prior to the commencement of the hearing. Decisions ~~A decision~~ of the board on petitions ~~a petition~~ for correction of an allocated assessment shall be completed on or before December 31 ~~of the year in which the relevant hearing was held~~.

Section 755

Transmission of estimates of total assessed values to county auditors. (a) On or before July 15, the Board shall transmit to each county auditor an estimate of the total unitary value and operating nonunitary value of state-assessed property in the county and of nonunitary state-assessed property in each revenue district in the county. An estimate need not be made for a revenue district that did not levy a tax or assessment during the preceding year unless the Board receives on or before January 1 preceding the fiscal year for which the levy is to be made a notice in writing of the proposed levy. The estimate shall be regarded as establishing the total assessed value of state-assessed property in the county and each revenue district in the county for the purpose of determining tax rates, subject only to such changes as may be transmitted on or prior to July 31. All information furnished pursuant to this section is at all times during office hours open to inspection of any interested person or entity.

(b) Notwithstanding subdivision (a), in making the estimate referred to in subdivision (a), the unitary value and nonunitary value of the property of regulated railway companies and property subject to subdivision (I) of section 98.9 shall be allocated by revenue district.

Section 756

Transmission of rolls to county auditor. (a) On or before July 31, the Board shall transmit to each county auditor a roll showing the unitary and operating nonunitary assessments made by the board in the county and the nonoperating nonunitary assessments made by the Board in each city and revenue district in the county; provided, however, that the roll need not show the assessments made by the Board in a revenue district which did not levy a tax or assessment during the preceding year. Such roll is at all times, during office hours, open to the inspection of any person representing any taxing agency or revenue district, or any district described in section 2131. If the roll does no show the assessments in a revenue district as herein provided and a notice of a proposed levy is furnished the Board in writing, on or before January 1 preceding the fiscal year for which the levy is to be made, the board shall furnish an estimate of the total

assessed value of nonoperating nonunitary state-assessed property in the district and shall transmit thereafter to the county auditor a statement of roll change showing the nonoperating nonunitary assessments made by the Board in the district.

(b) Notwithstanding subdivision (a), in making the roll referred to in subdivision (a), the unitary value and nonunitary value of the property of regulated railway companies and property subject to subdivision (I) of section 98.9 shall be enrolled by revenue district.

Section 758

If the Board roll has been transmitted to the local auditors, the Board may make an assessment of escaped property or a roll correction. At least 30 days prior to transmitting a statement of assessment of escaped property or making a roll correction, the Board shall notify the assessee whose property's full value has increased as a result of an escape assessment or roll correction of the assessed value of that property as it shall appear on the corrected roll. The notice shall be mailed to the assessee at its address shown in the records of the Board. The notice shall advise the assessee of the date by which and the place where a petition for reassessment may be filed. The date for filing the petition shall not be less than 50 days from the date of the mailing of the notice of value. The provisions of sections 741 and 744, inclusive, shall be applicable to petitions and hearings pursuant to this section except for the dates described for decisions of the Board.

Section 759

(a) If a timely petition for reassessment is not filed in accordance with the notice provided by the Board pursuant to section 758, an escape assessment or roll correction shall become final at the expiration of the period for filing a petition for reassessment specified by that notice.

(b) The Board may extend the period for filing a petition for reassessment once for a period not to exceed 15 days, provided a written request for the extension is filed with the Board prior to the expiration of the period for which the extension may be granted.

Section 11203

"Private railroad car." (a) "Private railroad car" includes any railroad rolling stock intended for the transportation of any persons, commodity, or material, operated on the railroads of this state, which car is owned by a person other than a railroad or the National Railroad Passenger Corporation. The car's Association of American Railroad's, or successor organization's, reporting mark shall be rebuttably presumed to be the mark of the car owner.

(b) "Private railroad car" does not include:

(1) Freight train or passenger train cars owned by railroad companies which are used or subject to use under the ordinary per diem agreement common to all railroads.

(2) Freight train or passenger cars handled under mileage or through line contract arrangements between railroad companies.

(3) Cars owned by or leased to any railroad company operating in this state, or by any railroad company operated as a part of the same railroad system as the company operating in this state, and used by the railroad company in the operation, maintenance, construction, or reconstruction of its property and assessed and taxed in this state as a part of the property of a railroad company operating in this state.

(4) Passenger train cars, other than those described in subdivision (b), that are privately owned and for which the owner pays the railroad a fee, regardless of how calculated, for transporting such cars.

(5) Any railroad rolling stock for which a railroad or the National Railroad Passenger Corporation is the lessee. For a leased car, the car's Association of American Railroad's, or successor organization's reporting mark is rebuttably presumed to be the mark of the lessee.

Section 11206

"Class of private railroad cars." "Class of private railroad cars" means the Association of American Railroad's, or successor organization's, one letter alpha component of its car type codes as contained in that organization's Exhibit D of the UMLER specification manual or successor exhibit.

Section 11251

Assessment of cars. Private railroad cars operated upon railroads into, out of, or through this state shall be assessed and taxed by the Board as prescribed in this part.

Section 11291

Property included in value of cars. The value of private railroad cars shall not include the car owner's tools, shop equipment, materials, supplies, or other like items of personal property customarily kept or maintained at fixed locations for use in repairing, improving, servicing, or operating the cars.

Section 11292

Depreciable life. In making the assessment, the Board shall value the cars by class based on the owner's acquisition cost, less depreciation. The depreciation shall be computed for these enumerated Association of American Railroad's, or successor organization's, car type groups on a straight-line basis with the indicated depreciable life schedules with a maximum of 80 percent depreciation allowed.

(a) Stack cars (alpha S): 22 years minus the age at acquisition.

(b) Lightweight, low profile intermodal cars (alpha Q): 22 years minus the age at acquisition.

(c) Flat cars (alpha F): 22 years minus the age at acquisition.

(d) Conventional intermodal cars (alpha P): 22 years minus the age at acquisition.

(e) Vehicular flat cars (alpha V): 22 years minus the age of acquisition.

(f) All other cars (all other alphas): 25 years minus the age at acquisition.

(g) Betterments: the remaining depreciable life of the car to which the betterment is applied.

Acquisition cost is defined as the expenditures required to be capitalized by generally accepted accounting principles.

Section 11293

Amount of cars. In making an assessment the Board shall determine the average number of each class of private railroad cars physically present in the state in the calendar year immediately preceding the fiscal year in which the tax is imposed upon the basis of car days. The Board shall multiply the average number so determined by the value of a car of that class as determined under section 11292 and use the product for the assessment of the cars.

Section 11294

Amount of cars; exclusion. In determining the averages required in section 11293, the Board shall exclude from the California factor car mileage, car days or such other data which occurs while cars are not qualified for revenue service and are in a repair facility in this state requiring and undergoing or awaiting remodeling, overhaul, renovation, conversion or repair which necessitates total labor in excess of 10 man-hours.

Car days excluded pursuant to this section shall not exceed 90 days per car unless the claimant provides substantiation of the necessity for the additional days in such form as prescribed by the Board.

PROPERTY TAX RULES

TITLE 18, PUBLIC REVENUES, CALIFORNIA CODE OF REGULATIONS

Rule 901. Property Statement

References: Section 826, Revenue and Taxation Code.
Section 15620, Government Code.

The property statement pertaining to state-assessed property provided for in section 826 of the Revenue and Taxation Code shall be filled with the Board between the lien date and 5 p.m. on March 1; provided that, on a showing of good cause and pursuant to a request made prior to March 1, the due date may be extended by the board for a period not exceeding 30 days.

Rule 901.5. Board Schedule

Reference: Sections 731, 732, 741, 742, 743, 747, 748, 749, 11338, 11339, 11353, Revenue and Taxation Code.

No later than November 30 each year the Executive Director shall provide to the Board a proposed schedule of dates that will govern the actions to be taken pursuant to sections 902 through 905 for the following calendar year. On Board approval, but no later than January 30 next following, the Executive Director shall inform all state assessees of the schedule adopted by the Board.

Rule 902. Unitary Property Value indicators and Staff Discussions

Reference: Section 721, 722, 723, 724, 725, Revenue and Taxation Code.

Each year the Valuation Division shall make capitalization rate studies and develop value indicators applicable tot he unitary property of each state assessee. A copy of the appropriate capitalization rate study and a summary of the calculations of the value indicators shall be provided by the Chief, Valuation Division, to the affected assessee on request. The assessee shall be informed that the staff will be available to discuss the data supplied.

Rule 903. Discussion with Board of Unitary Property value Indicators

Reference: Sections 721, 722, 723, 724, 725, Revenue and Taxation Code.

State assessees will, at the discretion of the Board, be afforded an opportunity to discuss the value of their unitary property at a public meeting. The discussion may relate to any information bearing on the value of the property as well as the staff-calculated value indicators. For the purposes of this discussion, the staff will not be required to provide value recommendations.

Rule 904. Unitary and Nonunitary Property Value Determinations and Petitions for Reassessment

Reference: Sections 721, 731, 732, 746, 749, 756, Revenue and Taxation Code.

(a) As soon as practical, the staff shall transmit unitary-value recommendations to the Board. Following this, but not later than May 31 each year, the Board will make and publicly announce individual value determinations. The Chief of the Valuation Division shall notify the state assessees of the values determined by the Board and the fact that they have 20 days from the date of the mailing of the notice to file their declaration of intent to petition for reassessment. The notice will also inform each assessee that if a declaration of intent is timely filed, the assessee has 30 days from the deadline for filing a declaration of intent to file a petition for reassessment. The notice shall be accompanied by a copy of an appraisal data sheet containing the staff value indicators and value recommendation to the Board.

(b) As soon as practical on or before the last day of June, the Chief of the Valuation Division shall notify the state assessees of the values of nonunitary property. This notice shall inform the assessees that they each have 20 days from the date of the mailing of their individual notice to

file a declaration of intent to petition for reassessment. The notice will also inform each assessee that if a declaration of intent is timely filed, the assessee has 30 days from the deadline for filing a declaration of intent to file a petition for reassessment.

(c) On or before the last day of June the Chief of the Valuation Division shall transmit notices of allocated assessed unitary values to each assessee. This notice will inform each assessee that it has 10 days from the date of mailing of the notice to petition the Board for reallocation of unitary values and that said petitions will be set for hearing and decisions rendered no later than July 31.

Rule 905. Assessment Electric Generation Facilities

Reference: California Constitution, article XIII, section 19; and section 721, Revenue and Taxation Code.

(a) Commencing with the assessment for the lien date for the 2003 assessment year, an electric generation facility shall be state assessed property for purposes of article XIII, section 19 of the California Constitution if: (1) the facility has a generating capacity of 50 megawatts or more; and (2) is owned or used by a company which is an electrical corporation as defined in subdivisions (a) and (b) of section 218 of the Public Utilities Code; or, the facility is owned or used by a company which is a state assessee for reasons other than its ownership of the electric generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.

(b) "Electric generation facility" does not include a qualifying small power production facility or a qualifying cogeneration facility within the meaning of Sections 201 and 210 of Title II of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. §§796(17), (18) and 824a-3) and the regulations adopted for those sections under that act by the Federal Energy Regulatory Commission (18 C.F.R. 292.101-292.602).

(c) For purposes of this section, "company" means:

(1) A person as defined in Revenue and Taxation Code section 19;

(2) A separate division or other functional unit of a business enterprise which is created and maintained to operate any electric generation facility, where the business enterprise is engaged in a primary business other than generating, transmitting, distributing or selling electricity to the public.

(d) If an electric generation facility is operated by a separate division or other functional unit of a business enterprise, as described in this rule, the business enterprise must maintain accounting and other records sufficient to distinguish the costs and revenues of the separate division or unit from other divisions and units of the business enterprise.

(e) As adopted on September 1, 1999 and effective November 27, 1999, this rule is applicable to define electric generation facilities subject to state assessment to and including December 30, 2002. As amended on November 28, 2001, and filed with the Secretary of State on May 14,

2002, this rule is applicable to define electric generation facilities subject to state assessment as of December 31, 2002 and thereafter.

~~An electric generation facility shall be state assessed property for purposes of article XIII, section 19 of the California Constitution if: (1) the facility was constructed pursuant to a certificate of public convenience and necessity issued by the California Public Utilities Commission to the company that presently owns the facility; or, (2) the company owning the facility is a state assessee for reasons other than its ownership of the generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.~~

Rule 1001. Annual Report

Reference: Section 11271, Revenue and Taxation Code.

The report required by section 11271 of the Revenue and Taxation Code of all persons whose private railroad cars operated upon the railroads in this state at an time during a calendar year shall be filed on or before the thirtieth day of April of the following year.

Rule 1003. Missing Private Railroad Car Count Data

Reference: Section 11293, Revenue and Taxation Code.

In determining the private railroad car count averages required by statute the Board may substitute for missing border crossing information that average length of stay in the state experienced by private railroad cars of the same class and assessee during the calendar year immediately preceding the year in which the tax is imposed. Border crossing information shall be deemed missing only when it cannot be submitted by the assessee.

CASES

Adams Express Company v. *Ohio State Auditor* (1897) 166 U.S. 185. In taxing properties located within its limits, a state may properly tax things united in use as a whole by reference to the productive use of the entire unit.

American Sheds, Inc. v. *County of Los Angeles* (1998) 66 Cal.App.4th 384. Certain intangibles, namely the operating permits and business enterprise value of a landfill, were not improperly subsumed in the valuation formula approved by the Board. In valuing property under section 110 (e), it may be valued by assuming the existence of intangible assets necessary to put the property to productive use. Thus, the assessor may assume the presence of a liquor license so that a bar's taxable property may be taxed as a bar and not at salvage value, (i.e., a warehouse); though the liquor license cannot be used to "enhance" the value of the property.

Bluefield Water Works and Improvement Company v. *Public Service Commission of The State of West Virginia, et al.* (1922) 262 U.S. 679. In valuing the property of a public utility corporation, the rates must be sufficient to yield a reasonable return on the value of the property at the time it is being used to render service.

California Portland Cement Co. v. *State Board of Equalization* (1967) 67 Cal.2nd 578. When there is insufficient market data available to ascertain the actual market value of the particular type of property, other factors such as replacement costs and income analyses, including the property's net earnings to be capitalized, may be employed.

The Cleveland, Cincinnati, Chicago & St. Louis Railway Company v. *Victor M. Backus* (1893)154 U.S. 439. The true value of a line of railroad is something more than the aggregation of the values of separate parts of it, operated separately; it is the aggregate of those values plus that arising from a connected operation of the whole.

County of Los Angeles v. *County of Los Angeles Assessment Appeals Board* (1993) 13 Cal.App.4th 102. Taxable possessory interests of car rental firms in public airports should be valued on the basis of the physical possession and exclusive use of their leased counters and reserved parking spaces, and not in the entire airport as a business premises. Some rights granted by the firms' agreements to do business at the airports were not possessory interests, but intangibles not subject to property tax.

County of Stanislaus v. *County of Stanislaus Assessment Appeals Board* (1989) 213 Cal.App.3d 1445. The appeals board erred in ruling that the company's entire franchises were nontaxable intangibles. The company's authority to use public rights-of-way is an assessable possessory interest in real property; and while the company's right to engage in the cable television business is not a part of this interest for assessment purposes, it can be considered in assessing the value of the possessory interest.

Cox Cable Company v. *County of San Diego* (1986) 185 Cal.App.3d 368. The interests of a cable television distribution company in franchise agreements granting the company the right to use and occupy public rights-of-way for the purpose of distributing its service are subject to property taxation since the company's use constitutes taxable possessory interests. A possessory interest may be the interest of either an easement holder or a mere permittee or licensee.

De Luz Homes, Inc. v. *County of San Diego* (1955) 45 Cal.2d 546 The absence of an actual market for a particular type of property does not mean that it has no value or that it may escape from the mandate of Constitution, article XIII, section 1, that all property shall be taxed in proportion to its value, but only that the assessor must then use such pertinent factors as replacement costs and analyses for determining valuation. In valuing a leasehold interest in exempt lands and improvements by the capitalization of income method it is improper, in computing the anticipated net income to be capitalized, to deduct from anticipated gross income the lessee's charges for rent, amortization of his investment, or payments of principal and interest on his mortgage debt. The proper method of valuing a possessory interest in a housing project at a permanent military installation is to deduct from annual anticipated gross income the operating and maintenance expenses and the amount required by the leased to be deposited to a replacement reserve, and to capitalize the difference for the remaining years of the lease at a rate which will allow for risk, interest, and taxes.

Dominguez Energy, L.P. v. *County of Los Angeles* (1997) 56 Cal.App.4th 839. The performance of environmental cleanup projects in conformity with an environmental protection statute may be treated as a "restriction imposed by government" within the meaning of section 402.1. Upon substantial evidence that the environmental cleanup will not be deferred to the end of the economic life of the property, clean up costs attributable to oil and gas operations should be recognized as nonrecurring capital expenditures within the cash flow. Environmental remediation costs that are likely to occur at abandonment should be treated as abandonment costs in the cash flow.

Firestone Tire and Rubber Company v. *County of Monterey* (1990) 223 Cal.App.3rd 382. Although the cost of pollution cleanup that reduces the fair market value of the property may form the basis for a reduction in the property's valuation under section 110, there was insufficient evidence to establish that the assessor knew or should have known that the plant was contaminated on the date the assessor's valuation of the plant was made.

GTE Sprint Communications Corporation v. *County of Alameda et al* (1994) 26 Cal.App.4th 992 Unit of taxation of public utilities and railroads is properly characterized as the taxation of property as a going concern, not as the taxation of real property or personal property, or even a combination of both. Under the unit taxation method, the Board considers the earnings of the property as a whole, and does not consider, less still assess, the value of any single real or personal asset. The valuation methodology used by the Board to assess tangible property was invalid, because it did not satisfactorily account for the value of the company's intangible assets. Intangible assets are not subject to property taxation, although their value may be included in the value of otherwise taxable tangible property. The Board erred in assuming that unit valuation, especially when calculated by the capitalized earnings ability method, necessarily taxed only the intangible values as they enhanced the tangible property.

ITT World Communications, Inc. v. County of Santa Clara (1980) 101 Cal.App.3d 246. The State Board of Equalization was free to alter its method of assessing public utility property subject to requirements of fairness and uniformity, and its abandonment of RCNLD as a ceiling was not arbitrary, in excess of discretion, or in violation of the standards prescribed by law. The Board's capitalization of income method of valuation was proper and did not result in an unconstitutional tax on plaintiff's franchise, even though the value arrived at by that method might exceed RCNLD. The Board's prior use of RCNLD did not have the status of a regulation that could be repealed only by pursuing statutory proceedings, and was not a policy that had been consistently acquiesced in by the Legislature and recognized by the courts so as to require legislation to change it.

ITT World Communications, Inc. v. *City and County of San Francisco et al.* (1985) 37 Cal.3d 859. California Constitution, article XIII, section 19, requiring public utility property to be "subject to taxation to the same extent and in the same manner as other property," does not require utility property to be valued on the same basis as other property, and therefore does not require the application of the valuation rollback provisions in California Constitution, article XIII A, section 2(a) to unit taxation of public utility property. The valuation rollback

provision is limited by its terms to locally assessed real property. Article XIII, section 19, simply specifies that public utility property be levied on at the same rate as locally assessed property.

Los Angeles SMSA Limited Partnership v. *State Board of Equalization* (1992) 11 Cal.App.4th 768. Market value for assessment purposes is the value of property when put to beneficial or productive use. One of the primary objectives of the system of unit taxation of public utility property is to ascertain and reach with the taxing power the entire real value of such property. It has long been recognized that public utility property cannot be regarded as merely land, buildings and other assets. Rather, its value depends on the interrelation and operation of the entire utility as a unit. Unit taxation is properly characterized not as the taxation of real property or personal property or even a combination of both, but rather as the taxation of property as a going concern.

Madonna v. County of San Luis Obispo (1974) 39 C.A.3d 57. Where there was no evidence that supported the assessment of improvements (a motel, restaurant and shops) based on a capitalized income approach that included enterprise value, and the board rejected two sets of valuation data that were supported, the Board acted on speculation and conjecture in determining the assessments. Such action of the Board was characterized as arbitrary and capricious, entitling the taxpayer to recovery of attorney's fees.

Michael Todd Company, Inc. v. *County of Los Angeles et al.* (1962) 57 Cal.2nd 684. The market value for assessment purposes is the value of property when put to beneficial use and is not the residual value remaining when the property is reduced to its constituent elements (e.g., a file negative should be valued as a motion picture, not merely as film). The absence of an "actual market" for a particular type of property does not mean that the property has no value, but only that the assessor must utilize other pertinent factors such as replacement cost and income analysis in making the valuation.

Norfolk and Western Railway Company et al. v. *Missouri State Tax Commission et al.* (1968) 390 U.S. 317. Any formula used in connection with the assessment of state taxes on an interstate enterprise must bear a rational relationship, both on its face and in its application, to property values connected with the taxing state; and a state is not permitted, under the shelter of an imprecise allocation formula, or by ignoring peculiarities of a given enterprise, to project its taxing power plainly beyond its borders.

Roehm v. *County of Orange* (1948) 32 Cal.2nd 280. The California Constitution contains a grant of power to the Legislature to provide for the assessment, levy, and collection of taxes, but it does not grant power to provide for the taxation of intangible assets other than those listed. Liquor licenses are not subject to ad valorem taxation as personal property , since they are not included in the list of intangibles specified.

Shubat v. *Sutter County Assessment Appeals Board* (1993) 13 Cal.App.4th 794. The right of a cable television company to do business, as well as the "enterprise value" of it as a going concern, has a separate value. Thus, the Board's method of allocating one-third of the residual value, after

assigning amounts to the tangible assets, to the possessory interest and the remainder to other nontaxable intangibles, was reasonable under the circumstances.

South Bay Irrigation District v. *California-American Water Company* (1976) 61 C.A.3d 944. Fair market value, that is, what a willing buyer would pay in cash to a willing seller, is the measure of just compensation in an action in eminent domain brought by a city to condemn for public use a privately owned waterworks system operating as a public utility. It is not improper to attach greater weight to the capitalization of income method of determining market value than to other methods proposed.

Southern California Telephone Company v. *County of Los Angeles* (1941) 45 Cal.App.2d 111. It is the function of a central assessment agency like the State Board of Equalization, to evaluate public utility property as a whole in order to assure the assessment of those values which cling to the entire property as a unit, and in order to assure the assessment of the same type of property at uniform value throughout the state. The very fact of segregation of such assessments from that of other property indicates an intention that the central assessment might be different from the values of the local assessor. In order for discrimination in assessment to occur, there must be two actions relating to different parties, and they must be performed by the same taxing agency.

Southern Pacific Pipe Lines, Inc. v. *State Board of Equalization* (1993) 14 Cal.App.4th 42. While article XIII, section 19 of the Constitution allows for the unit taxation of all public utility property, only those items deemed to constitute a private, intercounty pipeline may be assessed by the Board, including enumerated mechanical parts, fittings, and tanks necessary to the pipeline's operation. Real property interests, land, and rights-of-way, are excluded from the definition of a pipeline. Similarly, specific facilities, including a products plant, a wharf and marine terminal, engaged in multiple uses were not essential to the operations of intercounty pipeline that terminated there, and thus, were not part of the pipelines which the Board could assess.

GLOSSARY

Abnormal Costs	Amounts recorded in the property accounting records that are greater than what is typically expected in the construction or acquisition of a particular property; for example, costs incurred to correct construction flaws.
Accelerated Depreciation	A method of accruing greater depreciation expense in the early years of a property's life and less in the later years.
Accumulated Depreciation	The total depreciation recorded on, or charged against, an asset since its acquisition; a contra account deducted from the original cost of an asset on the balance sheet.
Ad Valorem Tax Component	The part of the total capitalization rate that reflects the property taxes that a hypothetical purchaser would incur on purchase of the subject property. The component is expressed as a relationship between the expected annual property tax expense and value.
Allowance for Funds Used During Construction (AFUDC)	A component of construction cost for a capital project representing the cost of financing the project during its construction.
Amortization	The process of retiring a debt or recovering a capital investment through scheduled, systematic repayment of principal; a program of periodic contributions to a sinking fund or debt retirement fund.
Annuity	A periodic series of obligatory payments; an annuity can be level, increasing, decreasing, or a combination thereof.
Anticipated Operating Expenses	The amount of future annual expenses anticipated, or expected, from the operation of property by a hypothetical purchaser.
Anticipated Operating Revenue	The amount of future annual revenues anticipated, or expected, from the operation of property by a hypothetical purchaser.
Apportionment to Intrastate Jurisdiction	The process of assigning a portion of a state unit value or state statistic or company statistic to geographical areas within a state, usually tax levying districts or tax-rate areas. Also called intrastate allocation.
Appraisal Unit	The unit of property that is typically bought or sold in the market.
Assessment Ratio	The relationship of assessed value to market value or to some other statutory value such as actual value, true cash value etc.

Band of Investment	A technique in which the capitalization rates attributable to components of a capital investment are weighted and combined to derive a weighted-average rate attributable to the total investment. In the context of corporate finance, called the weighted average cost of capital.
Basic Capitalization Rate	The rate of return on an investment necessary to attract investors; also known as the return on investment, or yield rate typically computed by use of the band of investment method. The basic capitalization rate does not include any adjustment for capital recapture or taxes.
Bond Discount	A dollar discount to the face value of a bond due to a market interest rate greater than the bond's coupon rate, or stated rate of interest.
Bond Premium	A dollar premium to the face value of the bond due to issuing costs or a market interest rate less than the bond's coupon rate, or state rate of interest.
Book Cost	The amount in dollars of an asset as it is carried in the accounting records of a firm. The original cost of an asset.
Book Value of an Asset	Capitalized, or book, cost less its accumulated (accounting) depreciation.
Capital Structure	The manner in which a business entity is financed; the mix, or relative proportions, of equity and debt used to finance the entity.
Capitalization Process	The procedure of converting income into value.
Capitalization Rate	Any rate used to convert income into an indicator of value; a ratio that expresses a relationship between income and value.
Cash Equivalent	Price of a property expressed in terms of cash, as distinguished from a price expressed, all or in part, in terms other than cash.
Cash Flow	The case receipts and cash expenditures associated with a project or investment.
Certificate of Public Convenience and Necessity	A grant of authority from a state or federal regulatory commission authorizing a company to render a public utility service, usually specifying the area and other conditions of service.
Common Carrier	An individual, corporation, or entity engaged in transporting persons, goods, or messages for compensation over a regular route, on a certain schedule, or at a published rate, all of which are usually subject to government regulation.

Comparative Sales Approach The technique of valuing properties by comparing them with similar properties that have been sold on a specified date. The comparative sales approach requires the sale of a sufficient number of similar properties within a specified period so that their characteristics and sales prices can be compared. It is based on the principle of substitution, which assumes that buyers would not pay more, and sellers would not accept less, for properties that are similar to, or have comparable utilities, to those that are sold in the same period.

Cost The expenditure required to develop and construct an improvement or acquire real and personal property.

Debt An obligation to repay a specified amount of money at a specified time. Long-term debt is considered to be a permanent part of the capital used by a firm.

Deferred Credits Miscellaneous long term liabilities. Often is a catchall account for long term liabilities that do not fit into any other liability category and are not material enough individually to constitute a separate category.

Deferred Income Taxes Accrued income tax credit or accrued income tax charge arising from the use of different accounting methods for financial and income tax reporting. To conform to regulatory requirements, public utilities generally use straight-line depreciation for financial accounting purposes. However, to minimize income tax liability, accelerated depreciation is generally used for income tax reporting. The use of different depreciation methods creates a tax timing difference known as deferred income taxes.

Depreciation

In accounting: the expense charged to amortize the historical cost of an asset over its useful life; the allocation of the historical cost of an asset to the accounting periods over which the asset provides economic benefits.

In valuation or appraisal: a decrease in utility resulting in a loss in property value; the difference between estimated replacement or reproduction cost new as of a given date and market value as of the same date. There are three principal categories of depreciation identified in appraisal:

(1) Physical Deterioration. The loss in utility and value due to some physical deterioration in the property; considered curable if the cost to cure it is equal to or less than the value added by curing it.

(2) Functional Obsolescence. The loss in utility and value due to changes in the desirability of the property; attributable to changes in tastes and style or the result of a poor original design. Functional obsolescence is curable if the cost to cure it is equal to or less than the value added by curing it.

(3) External (or Economic) Obsolescence. The loss in utility and value due to an incurable defect caused by external negative influences outside the property itself.

Easement

An interest in real property that conveys the right to use a portion of another's property.

Economic Life

The period of time over which improvements to real property contribute to the total property value.

Economic Rent

The amount of rental income that could be expected from a property if available for rent on the open market, as indicated by the prevailing rental rates for comparable properties under similar terms and conditions; economic rent is distinguished from contract rent, which is the actual rental income for the subject property as specified in a lease; economic rent is also referred to as market rent.

Embedded Debt Cost

The average rate of interest that a company pays for its long-term debt. The amount of total interest paid on long-term debt during the year divided by the face value of the long-term debt outstanding at the year-end. The historical cost of debt.

Equity

The ownership interest in a business. The net worth of a business, its total assets minus its total liabilities The amount of money the owners have invested in common and preferred stock plus earnings of the business that have not been paid out as dividends.

Expense The gross dollars periodically paid out for materials or services necessary to production. Operating expenses mean direct and incidental expenses in carrying on the primary business, for example, expenses of an electric utility in producing electric revenues. (Also, see Property Tax Rule 8.)

Fair Return An amount of income authorized by a regulatory agency that is considered sufficient for a utility to attract necessary additional capital and at the same time render adequate service.

Fixed Expenses Expenses of a firm that do not vary in relation to changes in volume of output, for example, interest on borrowed funds, insurance, rent, property taxes or depreciation in some instances.

Form 10-K Report An annual report submitted by corporations to the Securities and Exchange Commission. A new schedule in the 10-K requires certain large corporations to report the replacement cost of their productive capacity, the depreciated replacement cost, and the annual depreciation expense as though it were on a replacement cost basis.

Form R-1 The annual reports of business operation filed with the Surface Transportation Board by class I railroads.

Fractional Method Separately valuing each item of property.

Franchise A privilege to do certain things not a common right of citizens generally that is conferred by government to an individual or corporation.

Functional Obsolescence A form of appraisal depreciation. The loss in utility and value due to changes in the desirability of the property; attributable to changes in tastes and style of the result of a poor original design. Functional obsolescence is curable if the cost to cure it is equal to or less than the value added by curing it.

Generally Accepted Accounting Principles (GAAP) Accounting concepts, standards, and procedures adopted and promulgated by the Financial Accounting Standards Board. An audit report contains the auditor's certification of whether or not a firm has followed GAAP in the preparation of its financial statements.

Gross Additions New property added to existing plant or improvements. Betterments added to existing plant or improvements. Usually reported in dollar amounts.

Gross Income Income from the operation of a business or the management of property, customarily stated on an annual basis. Gross income is income to the property from all sources. In an apartment property, for example, the gross income could be the sum of living unit rent, parking space rent, vending machine and laundry facility income. (Also, see Property Tax Rule 8.)

Historical Cost The total cost of a property when it was originally constructed or purchased.

Income	Money or other benefits stemming from the ownership of property, generally received on a monthly or annual basis. The word "income" used alone has no specific appraisal significance, but must be qualified – for example, gross income, net operating income, etc.
Income Adjustment Factor	An adjustment in the mathematical derivation of the percent good factor that reflects an allowance for the reduction in income from a property as it ages.
Income Approach	Any method of converting an income stream or a series of future income payments into an indicator of present value.
Income Influence Method	A method of allocating a sale price or stock and debt value of a business to its different segments or subdivisions, according to the contribution of each segment to the total income of the business.
Income Tax Component	The part of the total capitalization rate that reflects the income taxes that a hypothetical purchaser would incur upon purchase of the subject property. This component is expressed as a relationship between the expected annual income tax expense and value.
Indicator of Value	An estimate of the monetary worth of a specifically identified property (be it a single parcel of land or piece of equipment or an extensive corporate conglomerate) based on consideration of particular characteristics or attributes of the property. Among the most common indicators of value are those derived from cost, income, and comparative sales approaches to value.
Interest Rate	The rate of return on debt capital; the price paid for borrowing money.
Interstate Allocation	The process of assigning a portion of a unit value or system statistic to a state, assuming that the unit value or system statistic reflects multistate operations.
J Factor	An adjustment made to straight-line depreciation in the calculation of the income tax component that reflects the relative benefits or disadvantages of the use of modified accelerated cost recovery system depreciation for determining income tax liability.
Land Reversion	The market value of land at the end of the remaining economic life of the assets (other than land) in a limited-life capitalized earnings ability model. This value is discounted to the valuation date using the basic capitalization rate plus a component for ad valorem taxes.
Liabilities	Claims held by non-owners on the assets of a business. Liabilities are obligations that a business is obliged to pay before the claims of the owners can be satisfied.

Lien Date — All taxable property (both state and locally assessed) is assessed annually for property tax purposes as of 12:01 a.m. on January 1, which is called the lien date. It is referred to as the lien date because on this date the taxes become a lien against all real property assessed on the secured roll.

Life Study — A survey or study of property lives by property category.

MACRS — The modified accelerated cost recovery system of depreciation allowed by the Internal Revenue Code.

Main Track — Refers to the lines or routes of railroad, whether main line or branch line, as distinguished from yard track, side track, or passing track.

Market Value — Also referred to as full cash value or fair market value. It means the amount of cash or its equivalent that property would bring if exposed for sale in the open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other and both with knowledge of all the uses and purposes to which the property is adapted and for which it is capable of being used and of the enforceable restrictions upon those uses and purposes.

Net Additions — Gross additions less the retirements; usually reported in dollar amounts.

Net Book Value — The amount, in dollars, of an asset as carried in the accounting records of a business. The original cost of an asset less its accrued depreciation.

Noncapitalized Leased Property — Leased property that is not reflected as a liability on a company's balance sheet.

Nonunitary Operations — Income-producing activities of a public utility that are not essential to the provision of its public utility service. Assets owned or used by a public utility that are not essential to the provision of its public utility service are known as "nonunitary property."

Nonunitary Property — Property not assessed as part of the unit. (Also, see nonunitary operations.)

Nonutility Operations — Income-producing activities of a public utility not related to its primary public utility function.

Normal Costs — Costs typically expected in the construction or acquisition of a particular property type.

Obsolescence — The loss in property value from causes other than physical deterioration. Obsolescence is functional if circumstances internal to the property item render it less desirable; or economic if circumstances external to the property and beyond the control of the property owner render the property less desirable.

Original Cost	The cost of the property item to the present owner. Sometimes used as equivalent to historical cost.
Percent Good	The complement of depreciation; if a property is 20 percent depreciated, its percent good is 80 percent. Percent good refers to the portion of benefits remaining in an asset compared to the total benefits when new.
Present Value (PV)	The value of a future payment or series of future payments discounted to the valuation date or some other specified date.
Pre-tax Cash Flow	Cash flow plus payment for income taxes. When applied to "cash flow", the term "before-tax" refers only to income taxes.
R3 Survivor Curve	One of the asset retirement curves developed and published by the Engineering Department at Iowa State University.
Rate Base	The dollar amount established by a regulatory agency on which a return is allowed.
Rate of Capitalization	A ratio of income to value. There are many types of capitalization rates depending on the elements included in the rate - for example, interest; investment, or capital, recapture; ad valorem taxes; and income taxes.
Rate of Return	A general term used in several ways. May refer to the yield to an investor, either on equity investment or total property value. May refer to the ratio of net operating income, before-tax cash flow, or some other level of income to the total property value, the initial equity or total investment, or the average equity or total investment during a given period.
Recapture	The return of invested capital. Capital may be returned gradually in periodic income, all or in part in resale of the property, or both. Different capitalization techniques are often distinguished by different methods of capital recapture.
Remaining Economic Life	The estimated period during which the improvements will continue to contribute to a property's value.
Replacement Cost	The cost required to replace an existing property with a property of equivalent utility.
Reproduction Cost	The cost required to reproduce an exact replica of an existing property.
Return on Equity	The ratio calculated as (typically annual) earnings on common equity divided by the value of the interest in common equity.
Revenue	The gross dollars received for the product or service provided. Operating revenue means revenue from the primary operations of the business, for example, electric revenues of an electric utility.

Reversion	A lump sum monetary benefit from a property that an investor receives or expects to receive at the termination of an investment.
Risk	Uncertainty about the outcome of future events; uncertainty about the future profitability of investments or projects; the possibility of not receiving the projected income.
Single Life Method	In the individual, or single life method, the percent good is simply a relationship between the present worth of an income for the probable remaining life expectancy and the present worth of an income for the total life expectancy. The single life method assumes that the best estimate of the future life expectancy of the survivors of a group is the average of the group.
Straight-line Depreciation	In accounting, of the practice of charging equal annual amounts of book depreciation expense; in appraisal, an assumed equal annual amount of loss in value to the property reflected as an allowance for depreciation in the capitalization rate.
Summation Method of Valuation	The combining of fractional valuations into one value; for example, the addition of the estimated value of the structure to the estimated value of the land to produce an estimate of the total property value.
System	An integrated operation constituted by separate units that may be related operating entities themselves or individual property elements, such as machinery, buildings, land, and other property, used in the production of goods and services.
Taxable Possessory Interest	Taxable possessory interests are possessory interests (as defined in section 107 and Rule 20) in publicly owned real property. Excluded from the meaning of taxable possessory interests, however, are any possessory interests in real property located within an area to which the United States has exclusive jurisdiction concerning taxation. Such areas are commonly referred to as federal enclaves. [Rule 20 (b)]
Total Capitalization Rate	A capitalization rate that converts the income to be capitalized into a capitalized value. The rate includes the investors' perception of both return on and return of (i.e., capital recapture) of the investment and components for ad valorem property taxes and income taxes.
Trending Factor	An index number expressed in decimal form that estimates the change in some variable cost, for example, over a time interval. A trending factor is multiplied by historical cost to estimate reproduction or replacement cost new.

Uniform System of Accounts	A prescribed method of accounting adopted by a state regulatory agency, such as a Public Utilities Commission; or by a federal regulatory agency, such as the Civil Aeronautics Board, the Federal Communications Commission, the Federal Energy Regulatory Commission, or the Interstate Commerce Commission.
Unit Method of Valuation	The technique of valuing a group of property items as "one thing."
Unitary Operations	Income-producing activities of public utility essential to the provision of its public utility service. All property owned or used by a public utility and essential to the provision of its public utility service is known as "unitary property"
Variable Expenses	Expenses of a business that vary with changes in volume of output, such as outlays for fuel in the generation of electric power.
Working Cash	The amount of cash, or cash balance, required for payment of expenses that are due before the revenue is collected. Necessary for most firms because of the unavoidable timing difference between cash receipts and disbursements.
WSATA	Western States Association of Tax Administrators. WSATA is an association of tax administrators from twelve western states – Alaska, Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming. Primary goals of the association are to facilitate dialogue among tax administrators, industry representatives, and academicians; and to promote research concerning issues affecting state assessment.
Yield Rate	In state assessment also known as basic capitalization rate; see basic capitalization rate.

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STATE OF CALIFORNIA

BOARD OF EQUALIZATION

Unitary Valuation Methods

PROPERTY AND SPECIAL TAXES DEPARTMENT
VALUATION DIVISION

HAROLD M. HALE, JR., CHIEF

Preface

The California Constitution requires the Board of Equalization to annually assess property, except franchises, owned or used by regulated railway, telegraph, or telephone companies, car companies operating on railways in the state, and companies transmitting or selling gas or electricity. It also requires the Board to annually assess pipelines, flumes, canals, ditches, and aqueducts lying within two or more counties. The taxes are levied and collected in the same manner as for county-assessed properties. The Valuation Division of the Property Taxes Department provides the elected members with reasonable and timely estimates of the market value of property subject to the Board's state assessment jurisdiction. State-assessed property, except rail transportation property, is assessed at its fair market value or full value as of 12:01 a.m. January 1. In conformity with federal law, the assessed value for railroad operating property and nonunitary rail transportation property is limited to a percentage of the market value set by the Board.

This *Unitary Valuation Methods* book has been prepared by the Valuation Division to document the valuation models currently used by the Board's staff in the preparation of indicators of value. ~~It also provides a logical starting point for future discussions of the relevancy of the various models or specific aspects of these models. This is of particular importance as we move from an era of highly regulated utilities to one of deregulation.~~

As part of the process of producing th~~is~~e original (November 1998) manual, and subsequent revisions (March 2000 and March 2003), meetings were held with ~~industry and county representatives~~ interested parties. Conflicts regarding the content of the manual were identified and most were resolved. Those issues not resolved ~~through these meetings were presented for decision to the~~ were voted on by Members of the Board of Equalization after hearing testimony from interested parties and Board Staff. The results of the Board's action are reflected in this manual.

Harold M. Hale Jr., Chief
Valuation Division

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Historical Cost Less Depreciation (HCLD) Model

Overview

The Historical Cost Less Depreciation (HCLD) value indicator derivation includes the historical or original acquisition cost of all property less nontaxable items and property assessed elsewhere. This results in the taxable historical cost. The taxable historical cost is then reduced for the assessee's regulatory accounting depreciation of the taxable property. This results in the assessable HCLD. The value of any possessory interest and/or noncapitalized leased properties are added to arrive at the final HCLD value indicator.

HCLD is one of the more important indicators of value for closely regulated public utilities. The general practice of the California Public Utilities Commission (CPUC) and most other regulatory agencies is to use historical or original cost less depreciation (with various adjustments) as the rate base. The regulatory agencies establish a rate base and a rate of return; utilities are permitted to earn at this established rate on the rate base. Hence, it is logical that prospective buyers and sellers would see the rate base as a significant factor in formulating investment decisions. HCLD is much less important for valuing public utility properties that are not closely rate base regulated.

One of the major components in the development of the HCLD indicator is accounting depreciation. For most rate base regulated utilities, there may be several sets of accounting records that record depreciation. The set of records reflecting the depreciation (normally straight-line) allowed by the rate setting regulatory agency for rate or tariff-setting purposes is the proper depreciation figure to use for the HCLD. [1]

Many utilities that are subject to central assessment are not closely regulated for economic results and therefore, do not maintain a depreciation reserve based on regulatory accounting rules. In such cases, an HCLD value indicator based on the assessee's book depreciation may be useful as a point of reference for establishing a relationship between net book value and market value. This indicator is generally not given any weight in the value reconciliation process, however as the use of HCLD is limited primarily to rate base regulated utilities.

Appraisal depreciation in the form of obsolescence may be present in utility property and deducted from HCLD. Such deductions may be proper when the utility's economic income has been impaired and the rate or tariff-setting regulators have recognized such impairment.

Since it is the practice of ratemaking agencies to deduct deferred income tax liabilities from the rate base, an adjustment for deferred income taxes is appropriate. Although a prospective purchaser would not necessarily expect to earn a return on the portion of the property represented by the deferred income tax liability, the prospective purchaser would expect to recover the cost of the investment through the depreciation allowances included in the rates. Therefore, the adjustment should measure the impairment on the utility's revenue, using the time value of money.[2]

[1] California Code of Regulations, Public Revenue, Title 18, Property Tax Rule 3(d)
[2] California State Board of Equalization, Assessor's Handbook 502, page 147

Historical Cost Less Depreciation (HCLD) Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*HC1*	Historical Cost (all property)		$ 20,000,000
2				
3				
4	*HC2*	*Less: Nontaxable Items*	*$ 2,500,000*	
5	*HC2*	*Property Assessed Elsewhere*	*1,000,000*	
6	*L4 + L5*	*Total Nontaxable Items*		*3,500,000*
7				
8	*L1 - L6*	Total Taxable Historical Cost		$ 16,500,000
9				
10	*HC1*	*Less: Depreciation*		*7,500,000*
11				
12	*L8 - L10*	HCLD Taxable Value		$ 9,000,000
13				
14	*HC3*	*Plus: Possessory Interest*		*1,101,900*
~~14~~	~~*HC3*~~	~~*Plus: Possessory Interest*~~		~~*1,063,800*~~
15	*HC3*	*Noncapitalized Leased Property*		*1,000,000*
16				
17	*L12+L14+L15*	**HCLD**		**$ 11,101,900**
~~17~~	~~*L12+L14+L15*~~	~~**HCLD**~~		~~**$ 11,063,800**~~
18				
19	*HC4*	Adjustment for Deferred Income Taxes		1,000,000
~~19~~	~~*HC4*~~	~~Adjustment for Deferred Income Taxes~~		~~*575,333*~~
20				
21	*L17 - L19*	**Adjusted HCLD**		**$ 10,101,900**
~~21~~	~~*L17 - L19*~~	~~**Adjusted HCLD**~~		~~**$ 10,488,467**~~
22				
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40		Note: Appendix I addresses exempt intangibles.		

Historical Cost of Property and Depreciation

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Direct Costs		
2		Materials	$ 5,000,000	
3		Labor	4,500,000	
4		Associated Construction Cost (permits, site improvements,		
5		freight, sales tax, installation, etc.)	3,500,000	
6		Total Direct Costs		$ 13,000,000
7				
8		Indirect Costs		
9		Administrative Expenses	$ 2,500,000	
10		Financing Cost	1,000,000	
11		Insurance and Taxes	1,000,000	
12		Marketing and Sales Expenses	2,500,000	
13		Total Indirect Costs		7,000,000
14				
15				
16	*L6 + L13*	**Historical Cost (All Property)**		**$ 20,000,000**
17				
18				
19				
20				
21				
22				
23				
24				
25				
26				
27		Depreciation (all property)		$ 8,250,000
28				
29		*Less: Depreciation for Nontaxables*		*500,000*
30		*Depreciation for Property Assessed Elsewhere*		*250,000*
31				
32	*L27 - L29 - L30*	**Depreciation for Taxable Property**		**$ 7,500,000**
33				
34				
35				
36				
37				
38				
39				
40				

Historical Cost (All Property) and Depreciation

Historical Cost of Property

For rate base regulated properties, the historical cost for appraisal purposes should be similar to the property cost required to be included on the utility's accounting records and reports to the regulator. Additionally, appraisal historical cost is increased for assessable property not included in the rate base and is reduced for nonassessable property included in rate base.

For non-rate base regulated properties, historical cost is the acquisition cost of the property when first acquired or constructed. Historical cost should also include all costs necessary to place the property into productive and beneficial use (i.e., direct costs and indirect costs). Abnormal costs should not be included, while normal costs for a typical owner should be included even though not incurred.[3, 4]

Depreciation

For appraisal purposes, depreciation is defined as the loss in value due to any cause, including internal and external factors.[5] The depreciation reserve subtracted from historical cost for rate base regulated utilities is based on the depreciation rates and methods established by the appropriate rate or tariff-setting regulatory agency.[6] The depreciation reserve for nontaxable items is removed from the total depreciation reserve. [7]

[3] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach
[4] The statement for a summarization of all reported cost is generally the Summary Control. The Summary Control shows the cost of all tangible property items, land, licensed vehicles, overhead (not spread elsewhere), and other costs.
[5] California State Board of Equalization, Assessor's Handbook 501, Chapter 6, Approaches to Value
[6] California Code of Regulations, Title 18, Public Revenue, Property Tax Rule 3(d)
[7] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach

Nontaxable Items and Property Assessed Elsewhere

Line No.	[a] Reference	[b] Description	[c] Amount
1		Nontaxable Items	
2		License Motor Vehicles	$ 800,000
3		Federal Enclave Property	300,000
4		Out of State Property	150,000
5		Computer Application Software	400,000
6		Business Inventory	250,000
7		Intangible Assets	300,000
8			
9		CIAC - Contribution in Aid of Construction	300,000
10			
11	*L2 thru L9*	**Total Nontaxable Items**	**$ 2,500,000**
12			
13			
14			
15			
16			
17			
18			
19			
20			
21			
22		Property Assessed Elsewhere	
23		Leasehold Improvements	$ 250,000
24		Nonutility Plant	250,000
25		Nonunitary Property	500,000
26			
27	*L23 thru L25*	**Total Property Assessed Elsewhere**	**$ 1,000,000**
28			
29			
30			
31			
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40			

Nontaxable Items and Property Assessed Elsewhere

In arriving at the historical cost of property to be assessed by the HCLD indicator, adjustments are required to remove property included in the HCLD indicator and exempt from taxation or taxed in another manner. First, there are nontaxable items, property that is specifically exempted by provisions of the Revenue and Taxation Code. Second, there are property items (e.g., contributions in aid of construction) that would have no value to a prospective purchaser of the utility. Third, certain types of property are assessed elsewhere. Property that is not an integral part of the utility operation may be classified and assessed as nonunitary property or may be assessed by a local county assessor.

Possessory Interest and Noncapitalized Leased Property

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Possessory Interest		
2		Rent or Franchise Payment		$ 262,450
3				
4	*Note*	Basic Capitalization Rate	13.280%	
5	~~*Note*~~	~~Ad Valorem Tax Rate~~	~~1.050%~~	
6	*Note*	Income Tax Component	8.120%	
7	$\frac{i}{(1+i)^{n}-1}$	Amount to Accumulate $1	2.419%	
8	*L4+L6+L7*	Total Capitalization Rate		23.819%
~~8~~	~~*L4+L5+L6+L7*~~	~~Total Capitalization Rate~~		~~24.670%~~
9				
10	*L2 / L8*	**Possessory Interest**		**$ 1,101,900**
~~10~~	~~*L2 / L8*~~	~~**Possessory Interest**~~		~~**$ 1,063,800**~~
11				
12				
13				
14				
15				
16				
17				
18				
19				
20		Noncapitalized Leased Property		
21		Historical Cost of Leased Property		$ 1,500,000
22		Less: Estimated Depreciation *(Based on a 15 year life)*		500,000
23				
24	*L21- L22*	**Noncapitalized Leased Property**		**$ 1,000,000**
25				
26				
27				
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35				
36				
37				

38 Note: The basic capitalization rate and income tax component used in the computations
39 above should match those used in the calculation of the capitalized earnings ability (CEA)
40 value indicator.

Possessory Interest and Noncapitalized Leased Property

Possessory Interest

A possessory interest is an interest in real property that exists as a result of the possession of, or a right to possess or occupy land and/or improvements unaccompanied by ownership of a fee simple or life estate in the property. A taxable possessory interest normally exists whenever a utility has exclusive right to possess tax-exempt, publicly-owned property. The utility benefits from the possession of this property right, and it is taxed for the value of the benefits it receives.[8]

A taxable possessory interest value is added to the value indicator because it is a real property right that is not generally represented on the balance sheet of the assessee's accounting records.[9]

A taxable possessory interest can be valued using any of three primary appraisal approaches: cost, income, or comparative sales. For mass appraisal, the most common approach used is the income approach because data regarding economic or market rents and franchise fee payments are readily available.

When valuing a possessory interest by the income approach, the present worth of the economic net income attributed to the property for the permitted use is discounted for the estimated term of possession. The discount rate is comprised of a basic capitalization rate, an income tax component, ~~an ad valorem property tax rate,~~ and the amount to accumulate $1 (calculated at the basic capitalization rate ~~plus the ad valorem tax rate~~). The formula is:

$$ER / (Y_o + ITC \text{ } \sout{+ ETR} + AAO)$$

where ER is the economic or market rent, Y_o is the basic capitalization rate, ITC is the income tax component~~, ETR is the effective ad valorem tax rate~~, and AAO is the amount to accumulate $1.

Noncapitalized Leased Property

Noncapitalized leased property is an additive to the unitary value indicator(s) because leased properties are not recorded on the utility's accounting records except for capitalized leased properties that should be reported the same as property purchased.[10]

Property used by an assessee under the terms of an operating lease should be included in the unitary value indicator when the property is part of the operating unit. If the lessor has property tax payment responsibility and the property is not part of the operating unit, the assessment is delegated to the local assessor. In the HCLD indicator, the operating leased property additive is determined by estimating the Historical Cost Less Depreciation of the property.

[8] Revenue and Taxation Code sections 107, 107.1, 107.4; Property Tax Rules 20~~-28~~-22, 27, 28.
[9] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach.
[10] The appraiser should ascertain whether the recorded costs represent market value.

Deferred Income Tax Adjustment to HCLD

(Replaces page 9 of Unitary Valuation Methods, March 2000)

Line No.	[a] Reference	[b] Description						[c] Amount
1		Property Related Deferred Income Tax Liability						$1,000,000
2								
3								
4		Example of the treatment of deferred income taxes in rate proceedings:						
5								
6		Year	1	2	3	4	5	Total
7		Beginning rate base	10,000	7,600	5,560	3,707	1,854	
8	*note 1*	Income before Taxes and Depr.	3,667	3,267	2,927	2,618	2,309	14,788
9	*note 2*	Tax Depreciation	3,000	2,100	1,633	1,633	1,634	10,000
10	*L8-L9*	Taxable Income	667	1,167	1,294	985	675	
11	*L10*0.4*	Income Tax Due	267	467	518	394	270	1,916
12	*note 3*	Book Depreciation	2,000	2,000	2,000	2,000	2,000	10,000
13	*L8-L12*	Book Income	1,667	1,267	927	618	309	
14	*L13*0.4*	Book Income Taxes	667	507	371	247	124	1,916
15	*L9-L12*	Difference in Depreciation	1,000	100	(367)	(367)	(366)	0
16	*L14-L11*	Difference in Tax	400	40	(147)	(147)	(146)	0
17	*L7-L12-L16*	Ending Rate Base	7,600	5,560	3,707	1,854	0	
18	*L8-L11*	Cash Flow	3,400	2,800	2,409	2,224	2,039	12,872
19	*note 4*	PW Factor @ 10%	0.9091	0.8264	0.7513	0.6830	0.6210	
20	*L18*L19*	PV of Cash Flows Yr.'s 1-5	3,091	2,314	1,810	1,519	1,266	10,000
21		PV of Cash Flows Yr.'s 2-5		2,545	1,991	1,671	1,393	7,600
22		PV of Cash Flows Yr.'s 3-5			2,190	1,838	1,532	5,560
23		PV of Cash Flows Yr.'s 4-5				2,022	1,685	3,707
24		PV of Cash Flows Yr. 5					1,854	1,854
25								
26								
27		Calculation of rate base:						
28		Historic Cost	10,000	10,000	10,000	10,000	10,000	
29		Accumulated Depreciation	2,000	4,000	6,000	8,000	10,000	
30		Deferred Income Tax Liability	400	440	293	146	0	
31	*L28-L29-L30*	Rate Base	7,600	5,560	3,707	1,854	0	
32								
33								
34								
35								
36	*note 1*	The pre-income tax return on rate base (net of all other expenses) required to achieve a 10% after-tax						
37		rate of return. The income tax rate is assumed to be 40%.						
38	*note 2*	150% declining balance accelerated depreciation switching to straight-line used for illustration purposes.						
39	*note 3*	Straight-line depreciation with no salvage value assumed.						
40	*note 4*	1/(1+i)^n, rounded to 4 decimal places						

Deferred Income Tax Adjustment to HCLD

This page superceded

Line No.	[a] Reference	[b] Description		[c] Amount	
1		Property Related Deferred Income Tax Liability	$	1,000,000	
2					
3		Average Remaining Economic Life of Depreciable Assets		15	yrs
4					
5	*L1 / L3*	Amount Recovered Annually *	$	66,667	
6					
7		Basic Capitalization Rate		13.28%	
8					
9		Present Value of $1,000,000 for 15 years @ 13.28%	$	424,667	
10					
11	*L1 - L9*	Adjustment to HCLD	$	575,333	
12					
13	*L11 / L1*	Percent of adjustment to deferred tax balance		58%	
14					
15					
16					
17		* Assumed that the cost will be recovered equally over the life of the			
18		of the existing assets.			
19					
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Deferred Income Taxes

The timing of certain expenses is not the same for financial accounting purposes and for federal and state income tax purposes. In general, income tax accounting rules allow for certain deductions, most notably depreciation, to be taken for income tax purposes prior to when the deductions are allowed for financial accounting purposes. This timing difference give rise to a balance sheet account called Deferred Income Taxes that records the amount of future income taxes due because deductions have already been taken for income tax purposes, but remain to be taken for financial accounting purposes.

The income tax expense allowed in the rate structure is the amount determined by financial accounting and not by the amount of income taxes actually paid. Regulatory agencies require that the deferred income tax liability be deducted from the HCLD in the calculation of the rate base. Therefore, a regulated company would not earn a return on property purchased with funds provided by the deferral of income taxes if this regulatory treatment of deferred taxes was prescribed. ~~Nevertheless, the company would be allowed to recover the cost of property purchased with funds provided by the deferral of income taxes through the depreciation component of the rates.~~

Regulatory agencies generally will not approve the sale of a utility property if the sale is disadvantageous to the ratepayers. A prospective purchaser of a utility property where deferred taxes were required to be deducted from the rate base would most likely assume that the same treatment would be required after the purchase. Therefore the HCLD indicator should be adjusted to reflect the earnings limitation imposed by the ratemaking treatment of the deferred income taxes. The amount of the adjustment should reflect the time value of money.[11]

The example on page 9 illustrates that the rate-making treatment of deferred income taxes effectively allows a company to recover only the income taxes actually paid and that the proper adjustment to the HCLD indicator reflecting the time value of money is 100% of deferred income taxes. Deferred income tax liabilities arising from non-property related items and depreciation of non-taxable property should not be included in the adjustment to the HCLD indicator. Please note that the present value of the expected future cash flows equals the beginning rate base for each year.

~~For mass appraisal purposes, the present value of the cash flows representing the recovery of the property purchased is assumed to be recovered equally over the average remaining life of the unitary property. This projected cash flow stream is discounted to present value using the basic capitalization rate as the discount rate. The difference between the present value of this stream of cash flows and the nominal amount of the property related deferred income tax liability represents the adjustment to the HCLD indicator for deferred income taxes.~~

~~Company specific calculations submitted by assessees will be considered and may replace the mass appraisal procedure described above~~.

[11] California State Board of Equalization, Assessor's Handbook 502, page 147.

Reproduction Cost Less Depreciation (ReproCLD) Model

Overview

The calculation of the Reproduction Cost Less Depreciation (ReproCLD) indicator is basically a two-step process. First, the reproduction cost new (ReproCN) is calculated by applying an index factor to the historical acquisition cost of property, segregated by year of acquisition. Second, the ReproCN is adjusted for normal depreciation by the application of a percent good factor to the ReproCN. The product of this calculation is the ReproCLD value indicator.

ReproCN is an estimate of the current cost to replace the existing property with a new property that is an *exact replica*, or virtually so, of the existing property. Data for the derivation of the ReproCN index factors can be obtained either from prices quoted by current vendors of the property or by applying an appropriate index factor to the historical or original acquisition cost of the property. [12] The use of published index factors is the preferred method when performing mass appraisals for property tax purposes.

Numerous trade publications provide index factors for the conversion of historical cost to ReproCN. The publishers of these index factors generally survey industry participants and equipment manufacturers and compare current prices to a historical cost database. The ratio of price change for a given year is the ReproCN index factor. In addition to historical cost, these factors should also include an allowance for freight-in, installation, overhead during construction, and other indirect costs of placing a piece of property into productive and beneficial use.

For appraisal purposes, depreciation is defined as the loss in value due to any cause, including internal and external factors.[13] Although depreciation that is calculated for the HCLD indicator follows the depreciation method(s) employed by the regulating authority, this is not the case for the depreciation calculation used in the derivation of the ReproCLD indicator. For the ReproCLD indicator, depreciation is the difference in value between a new identical substitute property and the existing property. This difference is recognized as the complement to the percent good factors. The Valuation Division conducts service life studies to assist in determining the appropriate percent good factors.

The usefulness of the ReproCLD in the appraisal process depends on whether or not the market recognizes an exact replica of the subject property as having adequate utility for the operational needs of a contemporary business. If there are economical substitutes (i.e., a property of lower cost or greater utility) for the property being appraised, the ReproCLD indicator may not be a reliable method to determine the fair market value of a subject property.

[12] California Code of Regulations, Public Revenue, Title 18, Property Tax Rule 6(b) and 6(c)
[13] California State Board of Equalization, Assessor's Handbook 501, Chapter 6, Approaches to Value

Reproduction Cost Less Depreciation (ReproCLD) Model

Line No.	Reference	Description	[c] Historical Cost	[d] Repro Cost Trend Factors	[e] Repro Cost New	[f] Percent Good Factor	[g] ReproCLD
					[c * d]		[e * f]
1	**ReproC1**	Historical Cost of Taxable Depreciable Property in Service					
2		(by year of acquisition)	$ 10,000,000	1.10	$ 11,000,000	0.50	$ 5,500,000
3							
4		*Plus Taxable Nondepreciable Property in Service:*					
5		*Land*	*1,000,000*	*Market Value*	*200,000*	*Market Value*	*200,000*
6	**ReproC4**	*Other*	*500,000*	1.00	*500,000*	1.00	*500,000*
7							
8	**ReproC4**	*Property Not in Service*	*250,000*	1.00	*250,000*	1.00	*250,000*
9							
10	**ReproC5**	*Plus: Possessory Interest*	-		*1,101,900*	1.00	*1,101,900*
~~10~~	~~**ReproC5**~~	~~*Plus: Possessory Interest*~~	-		~~*1,063,800*~~	~~1.00~~	~~*1,063,800*~~
11	**ReproC5**	*Noncapitalized Leased Property*	*800,000*	1.13	*904,000*	0.89	*804,560*
12							
13		**Value Indicator prior to consideration of Obsolescence**	$ 12,550,000		$ 13,955,900		$ 8,356,460
~~13~~		~~**Value Indicator prior to consideration of Obsolescence**~~	~~$ 12,550,000~~		~~$ 13,917,800~~		~~$ 8,318,360~~
14							
15		Additional or Extraordinary Obsolescence					*0*
15							
16		**Value Indicator adjusted for Additional or Extraordinary Obsolscence**					$ 8,356,460
~~16~~		~~**Value Indicator adjusted for Additional or Extraordinary Obsolscence**~~					~~$ 8,318,360~~
17							
18							
19							
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21							
22							
23							
24							
25							
26		Note: Appendix I addresses exempt intangibles.					

Historical Cost of Taxable Depreciable Property in Service

Line No.	[a] Reference	[b] Description	[c] Historical Cost	[d] Repro Cost Trend Factors	[e] Repro Cost New [c * d]	[f] Percent Good Factor	[g] ReproCLD [e * f]
1		Historical Cost of Taxable Depreciable Property in Service					
2		(by year of acquisition)	$ 8,000,000	1.10	$ 8,800,000	0.50	$ 4,400,000
3							
4		*Plus Other Taxable Depreciable Property In Service:*					
5		*Capitalized Interest Costs*	*600,000*	1.10	*660,000*	0.40	*264,000*
6		*Sales Tax, Freight, Installation, etc.*	*500,000*	1.10	*550,000*	0.40	*220,000*
7		*Capital Leases*	*400,000*	1.00	*400,000*	0.85	*340,000*
8		*Leased Acquisition Costs*	*300,000*	1.00	*300,000*	0.45	*135,000*
9		*Possessory Interests - Cost Based*	-	1.00	-	1.00	-
10		*Customer Premise Equipment*	*100,000*	1.00	*100,000*	0.40	*40,000*
11		*Other Adjustments*	*100,000*	1.90	*190,000*	0.53	*100,700*
12							
13		*Total Other Taxable Depreciable Property In Service*	2,000,000		2,200,000		1,099,700
14							
15	*L2 + L13 [Note]*	**Total Cost of Taxable Depreciable Property in Service**	**$ 10,000,000**	**1.10**	**$ 11,000,000**	**0.50**	**$ 5,500,000**
16							Rounded
17							
18							
19							
20							
21							
22							
23							
24							
25							
26							
27							
28		Note: The factors on *Line 15* are composites.					

Historical Cost of Property by Year of Acquisition

Historical cost is the original acquisition cost of the property when first acquired or constructed. Historical cost should also include all costs necessary to put the property into productive and beneficial use (e.g., direct costs and indirect costs). Abnormal costs should not be included, while normal costs for a typical owner should be included even if not incurred.[14, 15]

This historical cost of the property in service is supplied by the assessee on the property statement, Schedule B-1. Schedule B-1 requires the reporting of historical cost by year of acquisition and by property category. Because of differences in accounting systems, it is not always possible for assessees to report property cost by year of acquisition. In this case, the cost is reported by category and total cost only. When these costs are functionally related to the property in service, they will be valued for ReproCLD using associated trending and percent good factors.

[14] California Code of Regulations, Title 18, Public Revenue, Property Tax Rule 6 (b)

[15] The statement for a summarization of all reported cost generally is reported on the Summary Control. The Summary Control shall show the cost of all tangible property items, land, licensed vehicles, overhead (not spread elsewhere), and other costs.

Reproduction Cost Trend Factors

Line No.	[a] Reference	[b] Description	[c] Factor Code	[d] Year Acquired	[e] Reproduction Trend Factor
1		**Sample Trend Factors** (*by year of acquisition*)			
2		Buildings - Gas & Electric	B07	1975	2.52
3		Buildings - Local Telephone	B03	1980	1.95
4		Electric Plant Total with Generation	E19	1975	2.37
5		Gas Plant Total	G09	1975	2.67
6		Telecommunication Mechanical Equip. - Misc.	M01	1985	1.30
7		Outside Plant - Fiber Optic Cable	T19	1990	0.99
8		Central Office Equipment - Digital Switch	T02	1990	0.68
9		Telecommunication Furniture & Office Equip.	F03	1990	1.12
10					
11					
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Reproduction Cost Trend Factors

The ReproCN factors are the bases for converting the historical or original acquisition cost of property into current market/cost amounts. These index factors measure the relative price change of property over a given period of time. Reproduction cost index factors convert historical cost into an estimate of the current cost of reproducing an *exact replica* of a property. [16]

In developing reproduction cost trend factors, staff relies on the following sources which publish cost indexes for various property types: C.A. Turner, Boeckh, Engineering News Record, Marshall Valuation Service- Survey of Current Business Machinery & Equipment, California Department of Transportation - Highway Construction Price Index and Whitman, Requart & Associates - Public Construction Costs.

[16] California Code of Regulations, Public Revenue, Title 18, Property Tax Rule 6 (b)

Percent Good Factors

Line No.	[a] Reference	[b] Description	[c] Factor Code	[d] Year Acquired	[e] Average Life	[f] Percent Good
1		**Sample Condition Percent Good** *(by year of acquisition)*				
2		Buildings - Gas & Electric	B07	1975	25	37%
3		Buildings - Local Telephone	B03	1980	40	81%
4		Electric Underground Conductors	E03	1975	35	65%
5		Gas Transmission Mains	G08	1975	35	65%
6		Telecommunication Mechanical Equip. - Misc.	M01	1985	10	11%
7		Outside Plant - Fiber Optic Cable	T19	1990	19	74%
8		Central Office Equipment - Digital Switch	T02	1990	8	26%
9		Telecommunication Furniture & Office Equip.	F03	1990	10	40%
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Percent Good Factors

The percent good factors are used to determine the remaining value of a property, they are the complement of normal depreciation. The factors are the basis for adjusting the ReproCN into an indicator of fair market value. The factors used for a given property type are based on the expected economic life of that property type. The economic life of a property type or category is based on a service life study that surveys industry participants who own that type of property. [17]

In addition to economic life, there are four other variables that have an effect on percent good factors. These are: the rate of return, the method of calculation, the survivor curve, and the presence of an income adjustment factor. In the Valuation Division, these variables are determined as follows: rate of return annually established by Property Tax Department, single-life calculation method, R3 survivor curve and the use of an income adjustment factor reflecting a 10% decline over average life. [18]

Estimating loss in value to determine the fair market value of property based on the ReproCLD approach involves a mass appraisal method. The property statement is organized to facilitate the use of such a method, specifically the use of percent good factors. Service life studies (which help determine what percent good factors will be applied to a property type) can measure some, but not all, economic obsolescence.[19] Examples of economic obsolescence include: increased competition, unexpected technological innovation, legal limitations on use, and environmental factors.[20]

If an assessee properly and adequately documents additional or extraordinary obsolescence, it should be deducted from the ReproCLD value. Examples of acceptable methods to measure the amount of additional or extraordinary obsolescence include under appropriate facts, the cost to cure the obsolescence and the present value of the excess costs of operation caused by the obsolete property.

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[17] Valuation Division Operations Memorandum Number 12 - Conducting Service Life Studies.
[18] California State Board of Equalization, Assessor's Handbook 581.
[19] In addition to the percent good factor, the Valuation Division applies a *utility factor* to the ReproCLD for intercounty pipelines, pumps and boilers. The utility factor for pipelines measures obsolescence caused by usage substantially lower than the property's designed capacity. The purpose of the utility factor is to obtain an approximation of actual replacement cost based on current property usage.
[20] California State Board of Equalization, Assessor's Handbook 504, Pages 67-68.

Taxable Nondepreciable Property in Service and Property Not in Service

Line No.	[a] Reference	[b] Description	[c] Amount
1		Other Nondepreciable Property in Service - Other	
2		Other Land Rights	$ 100,000
3		Fiber Optic Rights of Way	200,000
4		Materials & Supplies	150,000
5		Assessable Directories	-
6		Non Current Gas	-
7		Fuel Stock	50,000
8			
9	*L2 thru L7*	**Total Other Nondepreciable Property in Service - Other**	**$ 500,000**
10			
11			
12			
13			
14			
15			
16			
17			
18			
19			
20		Property Not in Service:	
21		Future Use - Land	$ 25,000
22		Future Use - Other than Land	-
23		CWIP - Land	75,000
24		CWIP - Other than Land	150,000
25			
26	*L21 thru L24*	**Total Property Not in Service**	**$ 250,000**
27			
28			
29			
30			
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33			
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Taxable Nondepreciable Property in Service and Property Not in Service

Other Nondepreciable Property in Service - Property types can vary greatly given the industry groups being appraised.

Trend factors for this group of properties are generally set at one. Current market value should be used where it can be determined.

Property Not in Service - This property typically consists of Future Use Property and Construction Work in Process (CWIP).

Trend factors for this group of properties are generally set at one. Because these properties have suffered little depreciation or price change due to their recent acquisition, there is no adjustment required to the original purchase price. Preliminary engineering costs for a construction project should be included in the amount reported for CWIP in proportion to the percentage of project completion as of the lien date.

Rights of Way

Rights of Way Value - Rights of way can be defined as the right to use corridors of land between two or more points. These rights of way are used for railroad, highway, pipeline, or utility transmission line purposes. Telecommunications companies often acquire rights of way in easements owned by railroads (and others) to install fiber optic line conduits.

Easements represent a portion of the fee simple value of a real property parcel. An easement is an interest in real property that conveys use of a portion of an owner's property.[21] Easements, rights of way, and private and public restrictions affect property value.[22]

Rights of way generally are included in the unitary value of a public utility property, except pipeline ROWs that are locally-assessed. ROW values are an additive to the land value because ROWs are property rights that are generally not represented on the balance sheet of assessees' accounting records.[23]

If rights of way are available to a utility at no cost for the use of said right (e.g., public streets), then market value is considered to be zero. Therefore, staff only values the private ROW owned or used by public utility companies.

Calculation

Example - A state assessee reports to the Board the rights of way miles owned or used. In 1994, the Board determined the market value of fiber optic rights of way was $16,000 per mile.

ROW total market value = total private ROW miles x $16,000 per mile.

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[21] Appraisal Institute, *The Appraisal of Real Estate*, 11th edition, 146.
[22] Appraisal Institute, *The Appraisal of Real Estate*, 227.
[23] There may be rights that the assessee identifies as ROW, but in actuality are taxable possessory interests (e.g., fiber optic ROW located on the California aqueduct).

Possessory Interest and Noncapitalized Leased Property

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Possessory Interest		
2		Rent or Franchise Payment		$ 262,450
3				
~~4~~	*Note*	Basic Capitalization Rate	13.280%	
5	~~*Note*~~	~~Ad Valorem Tax Rate~~	~~1.050%~~	
6	*Note*	Income Tax Component	8.120%	
7	$\frac{i}{(1+i)^{\wedge} n-1}$	Amount to Accumulate $1	2.419%	
8	*L4 thru L7*	Total Capitalization Rate		23.819%
~~8~~	~~*L4 thru L7*~~	~~Total Capitalization Rate~~		~~24.670%~~
9				
10	*L2 / L8*	**Possessory Interest**		**$ 1,101,900**
~~10~~	~~*L2 / L8*~~	~~**Possessory Interest**~~		~~**$ 1,063,800**~~
11				
12				
13				
14				
15				
16				
17				
18				
19				
20		Unitary Noncapitalized Leased Property		
21		Cost of Leased Property		$ 800,000
22		Trend Factor		1.13
23	*L21 * L 22*	Reproduction Cost		$ 904,000
24		Percent Good		0.89
25	*L23 * L24*	**Reprodution Cost Less Depreciation**		**$ 804,560**
26				
27				
28				
29				
30				
31				
32				
33				
34				
35				
36				
37				
38		Note: The basic capitalization rate and income tax component used in the computations		
39		above should match those used in the calculation of the capitalized earnings ability (CEA)		
40		value indicator.		

Possessory Interest and Noncapitalized Leased Property

Possessory Interest

A possessory interest is an interest in real property that exists as a result of the possession of, or a right to possess or occupy land and/or improvements unaccompanied by ownership of a fee simple or life estate in the property. A taxable possessory interest normally exists whenever a utility has exclusive right to possess tax-exempt, publicly-owned property. The utility benefits from the possession of this property right, and it is taxed for the value of the benefits it receives.[24]

A taxable possessory interest value is added to the value indicator because it is a real property right that is not generally represented on the balance sheet of the assessee's accounting records.[25]

A taxable possessory interest can be valued using any of three primary appraisal approaches: cost, income, or comparative sales. For mass appraisal, the most common approach used is the income approach because data regarding economic or market rents and franchise fee payments are readily available.

When valuing a possessory interest by the income approach, the present worth of the economic net income attributed to the property for the permitted use is discounted for the estimated term of possession. The discount rate is comprised of a basic capitalization rate, an income tax component, ~~an ad valorem property tax rate,~~ and the amount to accumulate $1 (calculated at the basic capitalization rate ~~plus the ad valorem tax rate~~). The formula is:

$$ER / (Y_o + ITC \text{ } \sout{+ ETR} + AAO)$$

where ER is the economic or market rent, Y_o is the basic capitalization rate, ITC is the income tax component~~, ETR is the effective ad valorem tax rate~~, and AAO is the amount to accumulate $1.

Noncapitalized Leased Property

Noncapitalized leased property is an additive to the unitary value indicator(s) because leased properties are not recorded on the utility's accounting records except for capitalized leased properties that should be reported the same as property purchased.[26]

Property used by an assessee under the terms of an operating lease should be included in the unitary value indicator when the property is part of the operating unit. If the lessor has property tax payment responsibility and the property is not part of the operating unit, the assessment is delegated to the local assessor. In the ReproCLD indicator, the value of operating leased property is determined by the Reproduction Cost Less Depreciation of the property if the information is available. If the reproduction cost of the leased property cannot be determined from the information reported by the assessee, the appraiser may capitalize an economic lease payment over the remaining life of the leased property to estimate the leased property additive.

[24] Revenue and Taxation Code sections 107, 107.1, 107.4; Property Tax Rules 20-22, 27, 28.
[25] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach.
[26] The appraiser should ascertain whether the recorded costs represent market value.

Replacement Cost Less Depreciation (ReplCLD) Model

Overview

The calculation of the Replacement Cost Less Depreciation (ReplCLD) indicator is basically a two-step process. First, the replacement cost new (ReplCN) is calculated by applying an index factor to the historical acquisition cost of the property, segregated by year of acquisition. Second, the ReplCN is adjusted for depreciation by the application of a percent good factor to the ReplCN. The product of this calculation is the ReplCLD value indicator.

ReplCN is an estimate of the current cost to replace a property with a new property *of equivalent utility*, of the existing property. The cost to replace a property should include all economic costs necessary to prepare the property for productive and beneficial use. The Valuation Division currently obtains information for the derivation of ReplCN index factors from two sources: (1) Studies provided by industry participants and (2), studies performed by the Policy, Planning, and Standards Division (PPSD) of the Property Taxes Department. The studies performed by PPSD are limited at present to general purpose computer equipment and peripherals. The use of index factors applied to historical cost data is the preferred method of calculating ReplCN for mass appraisal purposes. The historical cost of property is adjusted (in the aggregate or by groups) for replacement cost level changes by multiplying the cost incurred in a given year by the appropriate replacement cost index factor.

ReplCN should reflect the current cost a knowledgeable person or company would pay if it were to be necessary to replace the subject property with a new property of equivalent utility. ReplCN is an excellent starting point for estimating the value of newer property not under rate of return regulation. This is because the property owner has the freedom, with competitive constraints, to adjust revenues to current costs based on market factors. Problems with the model include: (1) the difficulty in obtaining accurate replacement cost data, and (2) the subjectivity in selecting replacement property. These problems are minimized when the property to be appraised is relatively new.

While depreciation used for the HCLD indicator is the depreciation method(s) employed by the regulatory authority, this is not the case in the depreciation calculation for the ReplCLD indicator. For the ReplCLD indicator, depreciation is the difference in value between a new substitute property of equivalent utility and the existing property. This difference is recognized as the complement to the percent good factors. The Valuation Division conducts service life studies to assist in determining the appropriate percent good factors.

The usefulness of the ReplCLD depends on, whether accurate data can be collected in order to determine a mathematical relationship between the cost of an older property and the cost of newer property. This relationship, expressed as a mathematical ratio, is the ReplCN index factor. If this information is not available, or there is no consensus in the marketplace as to what constitutes equivalent utility, the ReplCLD indicator may not be a preferred method to determine the fair market value of a subject property.

If an assessee properly and adequately documents additional or extraordinary obsolescence, it should be deducted from the ReplCLD value. Examples of acceptable methods to measure the amount of additional or extraordinary obsolescence include, under appropriate facts, the cost to cure the obsolescence and the present value of the excess costs of operation caused by the obsolete property.

Replacement Cost Less Depreciation (ReplCLD) Model

Line No.	Reference	Description	[c] Historical Cost	[d] Repl Cost Trend Factors	[e] Repl Cost New	[f] Percent Good Factor	[g] ReplCLD
		Reference ---------->		**ReplC2**		**ReplC3**	
				*[c * d]*			*[e * f]*
1	**ReplC1**	Historical Cost of Taxable Depreciable Property in Service					
2		(by year of acquisition)	$ 10,000,000	0.75	$ 7,500,000	0.50	$ 3,750,000
3							
4		*Plus Taxable Nondepreciable Property in Service:*					
5		*Land*	*100,000*	*Market Value*	*200,000*	*Market Value*	*200,000*
6	**ReplC4**	*Other*	*500,000*	1.00	*500,000*	1.00	*500,000*
7							
8	**ReplC4**	*Property Not in Service*	*250,000*	1.00	*250,000*	1.00	*250,000*
9							
10	**ReplC5**	*Plus: Possessory Interest*			*1,101,900*	1.00	*1,101,900*
~~10~~	~~**ReplC5**~~	~~*Plus: Possessory Interest*~~			~~*1,063,800*~~	~~1.00~~	~~*1,063,800*~~
11	**ReplC5**	*Noncapitalized Leased Property*	*800,000*	1.11	*888,000*	0.89	*790,320*
12							
13		**Value Indicator prior to consideration of Obsolescence**	$ 11,650,000		$ 10,439,900		$ 6,592,220
~~13~~		~~**Value Indicator prior to consideration of Obsolescence**~~	~~$ 11,650,000~~		~~$ 10,401,800~~		~~$ 6,554,120~~
14							
15		Additional or Extraordinary Obsolescence					*0*
15							
16		**Value Indicator adjusted for Additional or Extraordinary Obsolscence**					$ 6,592,220
~~16~~		~~**Value Indicator adjusted for Additional or Extraordinary Obsolscence**~~					~~$ 6,554,120~~
17							
18							
19							
20							
21							
22		Note: Appendix I addresses exempt intangibles.					

Historical Cost of Property by Year of Acquisition

Line No.	[a] Reference	[b] Description	[c] Historical Cost	[d] Repl Cost Trend Factors	[e] Repl Cost New [c * d]	[f] Percent Good Factor	[g] ReplCLD [e * f]
1		Historical Cost of Property in Service					
2		(by year of acquisition)	$ 8,000,000	0.75	$ 6,000,000	0.50	$ 3,000,000
3							
4		*Plus Other Taxable Depreciable Property In Service:*					
5		*Capitalized Interest Costs*	*600,000*	0.75	*450,000*	0.39	*175,500*
6		*Sales Tax, Freight, Installation, etc.*	*500,000*	0.75	*375,000*	0.39	*146,250*
7		*Capital Leases*	*400,000*	0.75	*300,000*	0.85	*255,000*
8		*Leased Acquisition Costs*	*300,000*	0.75	*225,000*	0.40	*90,000*
9		*Possessory Interests - Cost Based*	*50,000*	1.00	*50,000*	0.80	*40,000*
10		*Customer Premise Equipment*	*50,000*	1.00	*50,000*	0.45	*22,500*
11		*Other Adjustments*	*100,000*	0.50	*50,000*	0.35	*17,500*
12							
13		*Total Other Taxable Depreciable Property In Service*	*2,000,000*		*1,500,000*		*746,750*
14							
15	*L2 + L13 [Note]*	**Total Cost of Taxable Depreciable Property in Service**	**$ 10,000,000**	**0.75**	**$ 7,500,000**	**0.5**	**$ 3,750,000**
16							Rounded
17							
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25		Note: The factors on *Line 15* are composites.					

Historical Cost of Property by Year of Acquisition

Historical cost is the original acquisition cost of the property when first acquired or constructed. Historical cost should also include all costs necessary to put the property into productive and beneficial use (e.g., direct costs and indirect costs). Abnormal costs should not be included, while normal costs for a typical owner should be included even if not incurred. [27, 28]

The historical cost of the property in service is reported by the assessee on the property statement, Schedule B-1. Schedule B-1 requires the reporting of historical cost by year of acquisition and by property category. Because of differences in accounting systems, it is not always possible for assessees to report property cost by year of acquisition. In this case, the cost is reported by category and total cost only. When these costs are functionally related to the property in service, they will be valued for ReplCLD using associated trending and percent good factors.

[27] California Code of Regulations, Title 18, Public Revenue, Property Tax Rule 6 (b)

[28] The statement for a summarization of all reported cost is generally reported on the Summary Control. The Summary Control shall show the cost of all tangible property items, land, licensed vehicles, overhead (not spread elsewhere), and other costs.

Replacement Cost Trend Factors

Line No.	[a] Reference	[b] Description	[c] Factor Code	[d] Year Acquired	[e] Replacement Trend Factor
1		Sample Trend Factors (*by year of acquisition*)			
2		Buildings - Gas & Electric	B07	1975	Not Available
3		Buildings - Local Telephone	B03	1980	Not Available
4		Electric Plant Total with Generation	E19	1975	Not Available
5		Gas Plant Total	G09	1975	Not Available
6		Telecommunication Mechanical Equip. - Misc.	M01	1985	1.30
7		Outside Plant - Fiber Optic Cable	Study	1990	0.79
8		Central Office Equipment - Digital Switch	Study	1990	0.43
9		General Purpose Computers	Study	1995	0.30
10		Telecommunication Furniture & Office Equip.	F03	1990	1.12
11					
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Replacement Cost Trend Factors

The ReplCN trend factors are the bases for converting the historical cost of property into current replacement cost levels. These factors measure the current cost of replacing the existing property with a substitute property having *equivalent utility*.

In developing replacement cost index factors, staff currently relies on two sources: (1) studies submitted by industry participants and (2) studies performed by the Policy Planning and Standards Division (PPSD) of the Property Taxes Department. The PPSD studies at present pertain only to general purpose computer equipment and peripherals.

Percent Good Factors

Line No.	[a] Reference	[b] Description	[c] Factor Code	[d] Year Acquired	[e] Average Life	[f] Percent Good
1		Sample Percent Good Factors (*by year of acquisition*)				
2		Buildings - Gas & Electric	B07	1975	25	37%
3		Buildings - Local Telephone	B03	1980	40	81%
4		Electric Underground Conductors	E03	1975	35	65%
5		Gas Transmission Mains	G08	1975	35	65%
6		Telecommunication Mechanical Equip. - Misc.	M01	1985	10	11%
7		Outside Plant - Fiber Optic Cable	Study	1990	19	74%
8		Central Office Equipment - Digital Switch	Study	1990	8	26%
9	*Note*	General Purpose Computers	Study	1995	5	
10		Telecommunication Furniture & Office Equip.	F03	1990	10	40%
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39		Note: The general purpose computer replacement trend factor on schedule ReplC2 takes into consideration				
40		the condition percent good. Accordingly, no separate percent good adjustment is required.				

Percent Good Factors

The percent good factors are used to determine the remaining value of a property, they are complements of physical deterioration and functional obsolescence. The factors are the basis for adjusting the ReplCN into an indicator of fair market value. The factors used for a given property type are based on the expected economic life of that property type. The economic life of a property type or category is based on a service life study that surveys industry participants who own that type of property. [29]

In addition to economic life, there are four other variables that have an effect on percent good factors. These are: the rate of return, the method of calculation, the survivor curve, and the presence of an income adjustment factor. In the Valuation Division these variables are determined as follows: rate of return annually established by Property Tax Department, single-life calculation method, R3 survivor curve and the use of an income adjustment factor reflecting a 10% decline over average life. [30]

Estimating loss in value to determine the fair market value of property based on the ReproCLD approach involves a mass appraisal method. The property statement is organized to facilitate the use of such a method, specifically the use of percent good factors. Service life studies (which help determine what percent good factors will be applied to a property type) can measure some, but not all, economic obsolescence.[31] Examples of economic obsolescence include: increased competition, unexpected technological innovation, legal limitations on use, and environmental factors.[32]

If an assessee properly and adequately documents additional or extraordinary obsolescence, it should be deducted from the ReplCLD value. Examples of acceptable methods to measure the amount of additional or extraordinary obsolescence include, under appropriate facts, the cost to cure the obsolescence and the present value of the excess costs of operation caused by the obsolete property.

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[29] Valuation Division Operations Memorandum Number 12 - Conducting Service Life Studies

[30] California State Board of Equalization, Assessor's Handbook 581.

[31] In addition to the percent good factor, the Valuation Division applies a *utility factor* to the ReproCLD for intercounty pipelines, pumps and boilers. The utility factor for pipelines measures obsolescence caused by usage substantially lower than the property's designed capacity. The purpose of the utility factor is to obtain an approximation of actual replacement cost based on current property usage.

[32] California State Board of Equalization, Assessor's Handbook 504, Pages 67-68.

Other Non-Depreciable Property in Service and Property Not in Service

Line No.	[a] Reference	[b] Description		[c] Amount
1		Other Nondepreciable Property in Service:		
2		Other Land Rights	$	100,000
3		Fiber Optic Rights-of-Way		200,000
4		Materials & Supplies		150,000
5		Assessable Directories		-
6		Non Current Gas		-
7		Fuel Stock		50,000
8				
9	*L2 thru L7*	**Total Other Non-Depreciable Property in Service**	**$**	**500,000**
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20		Property Not in Service:		
21		Future Use - Land	$	25,000
22		Future Use - Other than Land		-
23		CWIP - Land		75,000
24		CWIP - Other than Land		150,000
25				
26	*L21 thru L24*	**Total Property Not in Service**	**$**	**250,000**
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Other Nondepreciable Property in Service - Property types can vary greatly given the industry groups being appraised.

Trend factors for this group of properties are generally set at one. Current market value should be used where it can be determined.

Property Not in Service - This property typically consists of Future Use Property and Construction Work in Process (CWIP).

Trend factors for this group of properties are generally set at one. Because these properties have suffered little depreciation or price change due to their recent acquisition, there is no adjustment required to the original purchase price. Preliminary engineering costs for a construction project should be included in the amount reported for CWIP in proportion to the percentage of project completion as of the lien date.

Rights of way

Rights of way Value - Rights of way can be defined as the right to use corridors of land between two or more points. These rights of way are used for railroad, highway, pipeline, or utility transmission line purposes. Telecommunications companies often acquire rights of way in easements owned by railroads (and others) to install fiber optic line conduits.

Easements represent a portion of the fee simple value of a real property parcel. An easement is an interest in real property that conveys use of a portion of an owner's property.[33] Easements, rights of way, and private and public restrictions affect property value.[34]

Rights of way generally are included in the unitary value of a public utility property, except pipeline ROWs that are locally-assessed. ROW values are an additive to the land value because ROWs are property rights that are generally not represented on the balance sheet of assessees' accounting records.[35]

If rights of way are statutorily available to utilities at no cost for the use of said right (e.g., public streets), then market value is considered to be zero. Therefore, staff only values the private ROW's owned or used by public utility companies.

Calculation

Example - A state assessee reports to the Board the rights of way miles owned or used. In 1994, the Board determined the market value of fiber optic rights of way was $16,000 per mile.

ROW total market value = total private ROW miles times $16,000 per mile.

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[33] Appraisal Institute, *The Appraisal of Real Estate*, 11th edition, 146.
[34] Appraisal Institute, *The Appraisal of Real Estate*, 227.
[35] There may be rights that the assessee identifies as ROW, but in actuality are taxable possessory interest (e.g., fiber optic ROW located on the California aqueduct).

Possessory Interest and Noncapitalized Leased Property

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Possessory Interest		
2		Rent or Franchise Payment		$ 262,450
3				
4	*Note*	Basic Capitalization Rate	13.280%	
~~5~~	~~*Note*~~	~~Ad Valorem Tax Rate~~	~~1.050%~~	
6	*Note*	Income Tax Component	8.120%	
7	$\frac{i}{(1+i)^{\wedge}n-1}$	Amount to Accumulate $1	2.419%	
8	*L4 thru L7*	Total Capitalization Rate		23.819%
~~8~~	~~*L4 thru L7*~~	~~Total Capitalization Rate~~		~~24.670%~~
9				
10	*L2 / L8*	**Possessory Interest**		**$ 1,101,900**
~~10~~	~~*L2 / L8*~~	~~**Possessory Interest**~~		~~**$ 1,063,800**~~
11				
12				
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19				
20		Unitary Noncapitalized Leased Property		
21		Cost of Leased Property		$ 800,000
22		Trend Factor		1.11
23	*L21 * L 22*	Replacement Cost		$ 888,000
24		Percent Good		0.89
25	*L23 * L24*	**Replacement Cost Less Depreciation**		**$ 790,320**
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37				
38		Note: The basic capitalization rate and income tax component used in the computations		
39		above should match those used in the calculation of the capitalized earnings ability (CEA)		
40		value indicator.		

Possessory Interest and Noncapitalized Leased Property

Possessory Interest

A possessory interest is an interest in real property that exists as a result of the possession of, or a right to possess or occupy land and/or improvements unaccompanied by ownership of a fee simple or life estate in the property. A taxable possessory interest normally exists whenever a utility has exclusive right to possess tax-exempt, publicly-owned property. The utility benefits from the possession of this property right, and it is taxed for the value of the benefits it receives.[36]

A taxable possessory interest value is added to the value indicator because it is a real property right that is not generally represented on the balance sheet of the assessee's accounting records.[37]

A taxable possessory interest can be valued using any of three primary appraisal approaches: cost, income, or comparative sales. For mass appraisal, the most common approach used is the income approach because data regarding economic or market rents and franchise fee payments are readily available.

When valuing a possessory interest by the income approach, the present worth of the economic net income attributed to the property for the permitted use is discounted for the estimated term of possession. The discount rate is comprised of a basic capitalization rate, an income tax component, ~~an ad valorem property tax rate,~~ and the amount to accumulate $1 (calculated at the basic capitalization rate ~~plus the ad valorem tax~~). The formula is:

$$ER / (Y_o + ITC + \text{~~ETR +~~} AAO)$$

where ER is the economic or market rent, Y_o is the basic capitalization rate, ITC is the income tax component, ~~ETR is the effective ad valorem tax rate,~~ and AAO is the amount to accumulate $1.

Noncapitalized Leased Property

Noncapitalized leased property is an additive to the unitary value indicator(s) because leased properties are not recorded on the utility's accounting records except for capitalized leased properties that should be reported the same as property purchased.[38]

Property used by an assessee under the terms of an operating lease should be included in the unitary value indicator when the property is part of the operating unit. If the lessor has property tax payment responsibility and the property is not part of the operating unit, the assessment is delegated to the local assessor. In the ReplCLD indicator, the value of operating lease property is determined by the Replacement Cost Less Depreciation of the property if the information is available. If the replacement cost of the leased property cannot be determined from the information reported by the assessee, the appraiser may capitalize the lease payments (if economic) over the remaining life of the leased property to estimate the leased property additive.

[36] Revenue and Taxation Code sections 107, 107.1, 107.4; Property Tax Rules 20-22, 27, 28.
[37] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach.
[38] The appraiser should ascertain whether the recorded costs represent market value.

Capitalized Earning Ability (CEA) Models

Overview

The capitalized earning ability or income approach to value is used when the property under appraisal is typically purchased in anticipation of a money income and either has an established income stream or can be attributed a real or hypothetical income stream by comparison with other properties. It is the preferred approach for the appraisal of properties when reliable sales data are not available and the cost approaches are unreliable because the reproducible property has suffered considerable physical depreciation, functional obsolescence or economic obsolescence, is a substantial over- or underimprovement, is misplaced or is subject to governmental restrictions on income that are unrelated to cost.[39]

The income approach to value may be generally described as any method that converts future anticipated income into present value. The conversion process is commonly known as income capitalization. The income approach is premised on the assumptions that investors will buy and sell property based on the income it is expected to yield and that investors will discount expected income at its attendant risk rate over its anticipated duration.[40]

Application of the income approach requires estimating future annual income for a period of time and converting income into a value estimate by means of a capitalization rate or present worth factor. The critical ingredients of the approach are the amount of anticipated future income, duration of income, capitalization rate, and method of capitalization.

The Valuation Division uses two basic CEA models. The primary model used by the staff assumes that individual assets are replaced as they are retired. Under the perpetual life concept, the capital investment necessary to maintain a perpetual income flow is deducted from expected revenues. With the necessary capital investment, the income stream is sustained into perpetuity.

In certain factual situations where it is determined that replacements to the property will not be made, a limited life model is used. The estimate of the remaining life should be based on physical factors. For example, the expected remaining life of a depleting oil field served by a pipeline would establish the estimate of remaining economic life for that pipeline. The limited life model involves forecasting an income stream for a finite period of time and discounting the periodic cash flows at an appropriate rate to arrive at the present value. Any remaining benefits at the end of the finite life are discounted to present value and added to the capitalized income. The limited life CEA is further divided into two premises based on the shape of the income stream: the level-annuity capital recovery premise and the straight-line decline capital recovery premise. The level-annuity capital recovery is identical to a mortgage annuity payment, where the capital recovery begins at the lowest level at the beginning of the asset's life and grows as it ages. The straight-line decline capital recovery is similar to a straight-line depreciation, where the asset's recovery is the result of dividing its value equally over its estimated useful life. Care should be exercised by the appraiser in the selection of proper income steam premise. The level annuity capital recovery premise is not appropriate unless the prospective purchaser can reasonably expect that the level of revenue and expense anticipated will remain constant over the remaining life of the property.

The level of income capitalized in the level-annuity and the straight-line decline capital recovery models is the same. The capitalization rates are different to reflect the appropriate capital recovery premise.

[39] California Code of Regulations, Public Revenue, Title 18- Property Tax Rule 8
[40] Assessor's Handbook 501, Chapter 6, pages 93-94.

In addition to the CEA models discussed above, staff calculates a Net Liquidation Value (NLV) indicator for certain state assessees where the degree of economic obsolescence is such that the highest and best use of the assets would be to sell the assets for liquidation value rather than operate the company as a going concern. Historically, staff has calculated NLV for many of the "short line" railroad state assessees. This value indicator becomes meaningful when it is greater than the capitalized value of the projected earnings from the property under its current use. Staff views the NLV as the minimum value indicator for a state assessee.

The NLV value indicator assumes that the subject of the appraisal is not a viable business operation and that the most prudent economic course of action is to cease operations and dispose of the assets. The result of the NLV calculation is the present worth of the anticipated proceeds to be derived by breaking up the appraisal unit and selling off the land, improvements and personal property over time. The estimated selling price of each category of property is discounted to present value based on the estimated time required to sell or liquidate the property. The amounts for each category are then added to arrive at the NLV indicator.

Perpetual Life Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*CEA1*	Anticipated Operating Revenue		$ 50,000,000
2	*CEA2*	*Less Anticipated Operating Expenses*		*30,000,000*
3	*CEA3*	*Less Estimated Capital Replacement Expenditures*		*5,000,000*
4				
5	*L1 - L2 -L3*	Anticipated Net Income		$ 15,000,000
6	*CEA4*	*Less Working Cash Allowance*		*321,000*
7	*CEA5*	*Less Income Attributed to Intangibles*		*963,000*
8				
9	*L5 - L6 - L7*	Appraisal Income		$ 13,716,000
10	CEA6	Total Capitalization Rate		22.45%
11				
12	*L9 / L10*	Capitalized Earning Ability (CEA)		$ 61,095,768
13	*CEA7*	*Less Average Business Inventory*		*60,000*
14				
15	*L12 - L13*	Taxable CEA after Inventory Adjustment		$ 59,605,032
16	*CEA7*	Taxable Percentage		97.56%
17				
18	*L15 * L16*	Taxable CEA		$ 58,150,669
19				
20		Plus Taxable Property Additions		
21	*CEA8*	*Possessory Interest*	*$ 1,101,900*	
~~21~~	~~*CEA8*~~	~~*Possessory Interest*~~	~~*$ 1,063,832*~~	
22	*CEA10, L7*	*Construction Work In Progress Additive*	*500,000*	
23	*CEA10, L21*	*Future Use Property - Not in Rate Base*	*100,000*	
24		~~*Present Value of Transition Cost Recovery*~~	~~*400,000*~~	
25	*L21 thru L23*	Total Taxable Property Additions		*1,701,900*
~~25~~	~~*L21 thru L24*~~	~~Total Taxable Property Additions~~		~~*2,063,832*~~
26				
27	*L18 + L25*	**Total CEA Value Indicator**		**$ 59,852,569**
~~27~~	~~*L18 + L25*~~	~~**Total CEA Value Indicator**~~		~~**$ 60,214,501**~~
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42		Note: Appendix I addresses exempt intangibles		

Straight Line Capital Recovery Premise Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*CEA1*	Anticipated Operating Revenue		$ 50,000,000
2	*CEA2*	*Less Anticipated Operating Expenses*		*30,000,000*
3				
4	*L1 - L2*	Net Anticipated Income		$ 20,000,000
5	*CEA4*	*Less Working Cash Allowance*		*321,000*
6	*CEA5*	*Less Income Attributed to Intangibles*		*963,000*
7				
8				
9	*L4 - L5 - L6*	Appraisal Income		$ 18,716,000
10	CEA6	Total Capitalization Rate		28.93%
11				
12	*L9 / L10*	Capitalized Earning Ability (CEA)		$ 64,694,089
13	*CEA7*	*Less Average Business Inventory*		*60,000*
14				
15	*L12 - L13*	Taxable CEA after Inventory Adjustment		$ 64,634,089
16	*CEA7*	Taxable Percentage		97.56%
17				
18	*L15 * L16*	Taxable CEA		$ 63,057,017
19				
20		Plus Taxable Property Additions		
21	*CEA8*	*Possessory Interest*	*$ 1,101,900*	
~~21~~	~~*CEA8*~~	~~*Possessory Interest*~~	~~*$ 1,063,832*~~	
22	*CEA9*	*Present Worth of Land Reversion*	*67,100*	
23	*CEA10, L7*	*Construction Work In Progress Additive*	*500,000*	
24	*CEA10, L21*	*Future Use Property - Not in Rate Base*	*100,000*	
25	*L21 thru L24*	Total Taxable Property Additions		*1,769,000*
~~25~~	~~*L21 thru L24*~~	~~Total Taxable Property Additions~~		~~*1,730,932*~~
26				
27				
28	*L18 + L25*	**Total CEA Value Indicator**		**$ 64,826,017**
~~28~~	~~*L18 + L25*~~	~~**Total CEA Value Indicator**~~		~~**$ 64,787,949**~~
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42		Note: Appendix I addresses exempt intangibles		

Level Annuity Capital Recovery Premise Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*CEA1*	Anticipated Operating Revenue		$ 50,000,000
2	*CEA2*	*Less Anticipated Operating Expenses*		*30,000,000*
3				
4	*L1 - L2*	Net Anticipated Income		$ 20,000,000
5	*CEA4*	*Less Working Cash Allowance*		*321,000*
6	*CEA5*	*Less Income Attributed to Intangibles*		*963,000*
7				
8				
9	*L4 - L5 - L6*	Appraisal Income		$ 18,716,000
10	CEA6	Total Capitalization Rate		21.43%
11				
12	*L9 / L10*	Capitalized Earning Ability (CEA)		$ 87,335,511
13	*CEA7*	*Less Average Business Inventory*		*60,000*
14				
15	*L12 - L13*	Taxable CEA before Inventory Adjustment		$ 87,275,511
16	*CEA7*	Taxable Percentage		97.56%
17				
18	*L15 * L16*	Taxable CEA		$ 85,145,988
19				
20		Plus Taxable Property Additions		
21	*CEA8*	*Possessory Interest*	*$ 1,101,900*	
~~21~~	~~*CEA8*~~	~~*Possessory Interest*~~	~~*$ 1,063,832*~~	
22	*CEA9*	*Present Worth of Land Reversion*	*67,100*	
23	*CEA10, L7*	*Construction Work In Progress Additive*	*500,000*	
24	*CEA10, L21*	*Future Use Property - Not in Rate Base*	*100,000*	
25	*L21 thru L24*	Total Taxable Property Additions		*1,769,000*
~~25~~	~~*L21 thru L24*~~	~~Total Taxable Property Additions~~		~~*1,730,932*~~
26				
27				
28	*L18 + L25*	**Total CEA Value Indicator**		**$ 86,914,988**
~~28~~	~~*L18 + L25*~~	~~**Total CEA Value Indicator**~~		~~**$ 86,876,921**~~
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41				
42		Note: Appendix I addresses exempt intangibles		

Anticipated Operating Revenue

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Operating Revenue		
2		Operating Utility Revenue	$ 47,000,000	
3		Miscellaneous Operating Revenue	1,000,000	
4	*L2 + L3*	Total Operating Revenue		$ 48,000,000
5				
6		*Less: Uncollectible Revenue-Debit*		*500,000*
7	*L4 - L6*	Net Operating Revenue		$ 47,500,000
8				
9		*Plus: Rate Authorization Increase*		*3,500,000*
10	*L7+L9*	Adjusted Operating Revenue		$ 51,000,000
11				
12		*Less Disallowed Revenue:*		
13		*Nonrecurring Revenue*	*$ 200,000*	
14		*Nonutility Revenue*	*800,000*	
15	*L13+L14*	*Total Disallowed Revenue*		*1,000,000*
16				
17	*L10 - L15*	**Anticipated Operating Revenue**		**$ 50,000,000**
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Anticipated Operating Revenue

Estimates of anticipated revenue begin with an analysis of current annual gross revenues. Current financial statements, data included in property statement declarations, and a review of historical data are necessary for developing revenue estimates. Analysis of historical data is relevant only to assist in determining a reasonable estimate of future anticipated operating revenue that a prospective investor would expect.

Financial statements may disclose that recorded revenues should be modified to accurately reflect future expected revenues. For example, recent rate authorizations for revenue changes in the future will not be fully reflected in current operating statements and will require adjustments to reflect anticipated future operating revenue. Likewise, nonrecurring or nonutility revenues should be adjusted or deleted to reflect anticipated future operating revenue.

For stable properties, such as railroads, where little change in the physical operating unit occurs from year to year, an average of the previous five years of operating revenue may be an appropriate method to estimate future cash flows. For such properties, this averaging process smoothes the peaks and low points of the business cycle.

Anticipated Operating Expenses

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Operating Expenses:		
2		Maintenance and Repair Expense		$ 3,000,000
3		Rental Expense		500,000
4		Operators Wages		3,200,000
5		Contracted Operator Service Expense		1,300,000
6		Connecting Telephone Company Charges		1,000,000
7		Office Salaries		5,500,000
8		Sales and Advertising Expenses		2,500,000
9		Management Salaries		6,000,000
10		Office Supplies and Expense		1,000,000
11		Insurance Expense		1,800,000
12		Accounting, Legal and Other Services		1,000,000
13		Vehicle Expense		1,300,000
14		Noncapitalized Lease Rentals		300,000
15		Depreciation & Amortization Expenses		5,000,000
16		Taxes		2,200,000
17		Other Expenses		3,000,000
18				
19	L2 thru L17	Operating Expenses		$ 38,600,000
20				
21		*Less Disallowed Expenses:*		
22		*Nonrecurring Expenses*	*$ 900,000*	
23		*Expenses from Nonoperating Income*	*200,000*	
24		*Depreciation and Amortization Expenses*	*5,000,000*	
25		*Noncapitalized Lease Rentals*	*300,000*	
26		*Federal Income Tax*	*1,200,000*	
27		*Ad Valorem (Property) Tax*	*600,000*	
28		*State Income Tax*	*400,000*	
29				
30	L22 thru L28	*Total Non-Allowed Expenses*		*8,600,000*
31				
32				
33	*L19 - L30*	**Anticipated Operating Expenses**		**$ 30,000,000**
34				
35				
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Anticipated Operating Expenses

Estimates of anticipated operating expenses begin with an analysis of current annual operating expenses. Current financial statements along with data in property statement declarations are necessary for developing expense estimates, along with a review of historical data. Analysis of historical data is relevant only to assist in determining a reasonable estimate of future anticipated operating expenses that a prospective investor would expect.

The gross outgo should include current expenses and capital expenditures required to develop and maintain the estimated income.[41] Nonrecurring and nonoperating expenses should be adjusted or deleted to eliminate revenue distortions and to reflect anticipated future operating expenses. The proper level of income to capitalize is net income prior to any deductions for dividends, debt interest, corporate income taxes, ad valorem taxes, and depreciation.[42]

The amount of capital replacement required to perpetuate the income stream is allowed as an expense in the perpetual life model. For rate base regulated utilities, the appropriate level of capital replacement expenditures is book depreciation. The appropriate level of replacement expenditures for nonratebase regulated utilities can be estimated from a life study and the replacement cost of the assets. Because such studies do not exist for railroads, book depreciation expense is used as a surrogate for capital replacement expenditures unless more detailed information is available. Properly documented company specific replacement expenditure estimates may be used when they are determined to be more accurate than the mass appraisal estimates discussed above.

For stable properties, such as railroads, where little change in the physical operating unit occurs from year to year, an average of the previous five years operating expenses may be an appropriate method to estimate future cash flows. For such properties, this averaging process smoothes out the peaks and low points of the business cycle.

[41] California Code of Regulations, Public Revenue, Title 18 - Property Tax Rule 8.
[42] Western States Association of Tax Administrators Appraisal Handbook - Valuation of Utility and Railroad property page 41.

Estimated Capital Replacement Expenditures

Line No.	[a] Reference	[b] Description	[c] Amount
1		**For Rate Base Regulated Companies:**	
2			
3		**Book Depreciation**	**$ 5,000,000**
4			
5			
6			
7			
8			
9			
10		**For Non-Rate Base Regulated Companies:**	
11			
12	*CEA3a*	Replacement Cost	150,030,580
13			
14	*CEA3a*	Weighted Average Life New	18.9
15			
16	*L 12 / L 14*	**Estimate of Annual Capital Expenditures**	**$ 7,938,126**
17			
18			
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Replacement Capital Expenditures

The use of a perpetual life model requires that an appraiser allow as gross outgo an allowance for capital replacement expenditures necessary to develop and maintain the projected cash flows to perpetuity. The basis for the estimate of a capital replacement allowance varies depending on the type of regulation that a company is subject to. For a company that is rate base regulated, the amount of capital replacement expenditures that will allow the income stream to be maintained is based on book deprecation because the rates are established using book depreciation. If a reliable life study is available, an estimate of replacement cost expenditures for companies that are not rate base regulated can be developed by dividing the replacement cost (or reproduction cost, if replacement cost is not available) by the weighted average life new of the existing assets. Care must be taken by the appraiser to confine the estimate to only the replacement of existing assets and not include capital expenditures for growth. For this reason actual capital expenditures are often an inappropriate surrogate for the annual allowance of capital replacements.

Estimate of Remaining Economic Life

Line No.	Reference	[a] Description	[b] RCN	[c] Average Life	[d] Weighted RCN	[e] R3 Curve RCNLD	[f] REL * RCN
1		Fiber Optic Cable	$ 16,500,000	20	$ 330,000,000	$ 13,603,111	$ 313,500,000
2	*CEA3b*	Fixed Station Equipment	34,300,000	8	274,400,000	25,394,180	148,329,860
3		Furniture & Office Equipment	34,930,580	14	489,028,120	31,343,299	454,097,540
4		Buildings	64,300,000	27	1,736,100,000	8,780,430	1,337,440,000
5							
6		TOTALS	$ 150,030,580		$2,829,528,120	$ 79,121,020	$2,253,367,400
7							
8							
9							
10							
11							
12	*L6[d]*	Age Weighted RCN - New					$2,829,528,120
13							
14	*L6[b]*	Replacement Cost New					150,030,580
15							
16	*L12 / L14*	Average Weighted Life New					18.9
17							
18	*L14 / L16*	Estimate of Required Capital Replacement Expenditures					$ 7,938,126
19							
20							
21							
22	*L6[f]*	RCN Weighted REL					$2,253,367,400
23							
24	*L6[b]*	Replacement Cost New					150,030,580
25							
26	*L22 / L24*	Weighted Average REL					15.0
27							
28							
29							
30							

Estimate of Average Economic Life New and Remaining Economic Life

Each account's cost, by year of acquisition, is trended to RCN and the appropriate condition percent is applied to determine RCNLD. The age-weighted RCN is calculated by multiplying each year's RCN by the age as of the lien date. The weighted average life new can then be calculated by dividing the summation of the RCN times the average life new by the RCN.

The single life estimate of remaining economic life for each age class is determined by reference to the percentage good table. The remaining life for each age class is then multiplied by the RCN to weight each asset (or class of assets) appropriately. The weighted average Remaining Economic Life for the unit is then calculated by dividing the summation of the RCN-weighted remaining economic life by the RCN. Schedule 3b shows the calculation detail for the fixed station equipment account.

Fixed Station Equipment

Detailed Life and RCN Information

Line No.	[a] Year	[b] Cost	[c] T-6 Factor	[d] RCN	[e] Weighted RCN by Age	[f] Percent Good 8 yr life	[g] RCNLD	[h] REL	[i] REL X RCN
1	1997	8,750,000	1.00	8,750,000	8,750,000	89%	7,787,500	7	54,512,500
2	1996	14,700,000	1.02	14,994,000	29,988,000	78%	11,695,320	6	70,171,920
3	1995	0	1.03	0	-	67%	0	5	0
4	1994	10,150,000	1.04	10,556,000	42,224,000	56%	5,911,360	4	23,645,440
5									
6	Total	33,600,000		34,300,000	80,962,000		25,394,180		148,329,860
7									
8									
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Working Cash Allowance

Line No.	[a] Reference	[b] Description	[c] Amount
1		Anticipated Operating Expenses	$ 30,000,000
2			
3		18 Days or Approximately 5 Percent	5%
4			
5	*L1 * L3*	Projected Working Cash Requirement	$ 1,500,000
6			
7		Basic Capitalization Rate	13.28%
8			
9	*CEA 6a*	Income Tax Component	8.12%
10			
11	*L7 + L9*	Basic Rate plus Income Tax Component	21.40%
12			
13	*L5 * L11*	**Working Cash Allowance**	**$ 321,000**
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Working Cash Allowance

The return on working cash as measured by the basic capitalization rate is deducted from the income stream to remove nontaxable working cash from the CEA. This complies with the direction of Board Rule 8 (e) to exclude sufficient income from the amount to be capitalized to provide a return on working capital.

A working cash allowance is required to provide the owner with a return on funds provided to the business for the purpose of paying operating expenses in advance of receipt of offsetting revenues from its customers. Cash held for construction, purchases of stock, payment of dividends and interest on funded debt, income and ad valorem taxes, and non-cash expenses such as depreciation, do not qualify for inclusion in cash working capital. The utility's working cash requirement is predicated upon having sufficient cash balances to enable the company to make timely payments for purchase of goods, services and materials.

State assessees report to the Board the amount of working cash as determined by a lead-lag study in their latest request for a rate change to the appropriate regulatory commissions. If such information is not available, the assessee should report an estimate of its average working cash requirement. If no estimate is available, an estimate of the working cash allowance is calculated by the appraiser using the following calculation:

$Exp * 5\% * (Y_o + ITC)$

where Exp is the anticipated operating expenses, 5% equates to an 18 day working cash requirement, Y_o is the basic capitalization rate, and ITC is the income tax component.

Income Attributed to Intangibles

Line No.	[a] Reference	[b] Description	[c] Amount
1		Customer Base	$ 3,000,000
2			
3		Patents and Copyrights	1,500,000
4			
5	*L1 + L3*	Total Intangibles	$ 4,500,000
6			
7		Basic Capitalization Rate	13.28%
8			
9	*CEA 6a*	Income Tax Component	8.12%
10			
11	*L7 + L9*	Basic Rate plus Income Tax Component	21.40%
12			
13	*L5 * L11*	**Income Attributed to Intangibles**	**$ 963,000**
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42		Note: Appendix I addresses exempt intangibles	

Income Attributed to Intangibles

When income to be capitalized is derived from operating a property, sufficient income shall be excluded to provide a return on any nontaxable operating assets such as intangible items.[43,44]

After the value of the intangible items is determined, the amount of income to be excluded is calculated in the same manner as the allowance for working cash. The intangible value is determined by multiplying the value of the intangible items by the basic capitalization rate plus a component for income taxes.

[43] California Code of Regulations, Public Revenue, Title 18 - Property Tax Rule 8(e)
[44] California State Board of Equalization, Assessor's Handbook 502, at page 150 for a discussion of intangible assets

Total Capitalization Rate Calculation

Line No.	[a] Reference	[b] Description	[c] Perpetual Life	[d] Limited Life: Straight line Decline	[e] Limited Life: Level Annuity
1		Basic Capitalization Rate	13.28%	13.28%	13.28%
2					
3		*No recapture component for Perpetual Life*	0.00%		
4		*Recapture:*			
5		*1/REL for Straight line Decline*		6.67%	
6		*Sinking Fund Factor for Level Annuity*			2.22%
7					
8		*Property Tax Component*	1.05%	1.05%	1.05%
9					
10	*CEA6a, L27*	*Income Tax Component*	8.12%	7.93%	4.88%
11					
12	*L1 thru L10*	**Total Capitalization Rate**	**22.45%**	**28.93%**	**21.43%**
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Total Capitalization Rate Calculation

The income approach estimates future annual income and converts this income into a value estimate by means of a capitalization rate. Property Tax Rule 8 excludes property taxes, income taxes, and capital recovery from the definition of gross outgo in the computation of capitalized earnings values. These types of cash outflows are not included in gross outgo because the amount of the cash flow is dependent on the value of the property. The tax and depreciation expenses of the current owner of the property would not be appropriate estimates of a new owner's expenses. A component for these items is added to the capitalization rate to reflect the purchaser's amount of property taxes, income taxes, and recovery of the original investment.

The calculation of the total capitalization rate consists of four basic components: a basic capitalization (or yield) rate component, a recapture component, an ad valorem property tax component, and an income tax component.

The basic capitalization rate is derived by applying a weighted average of the yield rates for debt and for equity capital calculated by the band-of-investment method. The rates of debt and equity capital are weighted by the respective amounts of capital deemed most likely to be employed by prospective purchasers. The Valuation Division develops basic capitalization rates for all state assessees in the Board's annual Capitalization Rate Study.

The recapture component provides for a periodic recovery of invested capital in a wasting asset over a period of time. The level annuity capital recovery premise uses a sinking fund factor from compound interest tables. The straight line capital recovery premise uses a recapture component calculated by dividing one by the remaining economic life. The perpetual life model requires no component for recapture, because estimated capital replacement expenditures are allowed as operating expenses and the property value is presumed stable.

The property tax component consists of the cash outlay for property taxes that a prospective purchaser would anticipate. An average property tax rate is calculated for each state assessee.

The income tax component approximates the cash outlay for income taxes that a prospective purchaser would anticipate. The income tax component allows for both state and federal income taxes. This adjustment is required to convert the after-income tax yield rate developed in the capitalization rate study to a pre-income tax level.

Income Tax Component Calculation

Line No.	[a] Reference	[b] Description	[c] Perpetual Life	[d] Limited Life Straight Line	[e] Limited Life Level
1		Basic Capitalization Rate	13.28%	13.28%	13.28%
2		*Add: Recapture Rate*	*0.00%*	*6.67%*	*2.22%*
3					
4	*L1 + L2*	Capitalization Rate before Income Tax Adjustment	13.28%	19.95%	15.50%
5					
6					
7		Depreciation Rate (1/ REL)	0.00%	6.67%	6.67%
8	*CEA4b*	J Factor	0.00	1.04	1.04
9					
10	*L7 * L8*	Adjusted Depreciation Rate	0.00%	6.94%	6.94%
11					
12					
13	*L4 - L10*	Capitalization Rate - Adjusted	13.28%	13.01%	8.56%
14					
15					
16		*Debt Ratio*	20.00%	20.00%	20.00%
17		*Debt Rate*	7.42%	7.42%	7.42%
18					
19	*L16*L17*	*Interest per $ of Value*	1.48%	1.48%	1.48%
20					
21					
22	*L4-L10-L19*	Profit (after Corporate Income Tax) per $ of Value	11.80%	11.53%	7.08%
23		One minus Effective Income Tax Rate	59.25%	59.25%	59.25%
24					
25	*L22/L23*	Pre-Corporate Income Tax Profit per $ of Value	19.92%	19.46%	11.96%
26					
27	***L25 - L22***	**Corporate Income Tax per $ of Value**	**8.12%**	**7.93%**	**4.88%**
28					
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Income Tax Component

The basic capitalization rates developed in the annual Capitalization Rate Study are the prospective purchasers' required rates of return after payment of corporate income taxes. Taxes measured by income, such as the federal corporate income tax and the California corporate franchise tax, are excluded from the definition of gross outgo pursuant to Property Tax Rule 8 (c). Instead of allowing a deduction for income tax expenses in the cash flows, a component that provides for the income taxes of a prospective purchaser is added to the basic rate along with the components for recapture and property taxes. The income tax formula allows for the tax shield that interest payments and depreciation enjoy under the Internal Revenue Code.

The recapture component or capital recovery rate is added to the basic capitalization rate (which is an after income tax rate) to compute the total rate before income tax adjustment. The recapture rate used should be consistent with the underlying premise in the capitalization model used in the appraisal. If the appraiser projects a level terminal income stream the sinking fund factor, at the applicable basic rate and remaining economic life (REL), should be used. If a straight line declining income stream is projected, the recovery rate should be 1/REL. For a perpetual income model, no capital recovery rate should be added because the income stream already includes a cash outflow for capital replacements.

If material, the adjustment for the tax deductibility of depreciation is then accounted for by adjusting straight line or financial depreciation to reflect the benefits of accelerated depreciation as allowed by modified accelerated cost recovery system (MACRS). This is accomplished by multiplying the straight line depreciation rate by the J factor. Because the tax lives of used properties are generally not materially different from the remaining economic life of those properties, the 'J' factor is only calculated for a unit comprised entirely of new assets. The tax deductibility of interest paid on debt is computed by multiplying the ratio of debt in the capital structure by the interest rate.

The after corporate income tax profit per dollar of value is computed by deducting the depreciation and interest adjustments from the total capitalization rate before income tax adjustment. This is adjusted to a pre-tax value by dividing it by 1 less the effective tax rate.

The difference between the pre-tax and after tax profit represents the amount of projected income taxes expressed as a percentage of value. This represents the income tax additive to the basic capitalization rate.

J Factor Calculation

Line No.	[a] Reference	[b] Description	[c] Year 1	[d] Year 2	[e] Year 3	[f] Year 4	[g] Year 5	[h] Year 6	[i] Year 7	[j] Year 8	[k] Total
1		***Remaining Economic Life of 6.8 years for Demonstration Purposes***									
2											
3		MACRS %	14.29%	24.49%	17.49%	12.49%	8.93%	8.92%	8.93%	4.46%	100.00%
4	*L3*6.8*	Tax Depreciation	0.9717	1.6653	1.1893	0.8493	0.6072	0.6066	0.6072	0.3033	6.8000
5											
6		Financial Depreciation (straight line)	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	0.8000		6.8000
7											
8											
9											
10	*PW of L4*	Net Present Value of MACRS Deductions									4.4676
11											
12	*PW of L6*	Net Present Value of Financial Depreciation									4.3008
13											
14	*L10/ L12*	**J Factor**									**1.04**
15											
16											
17											
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J Factor

The "J factor" represents an adjustment to financial depreciation rate used in the computation of the income tax component to adjust for the recognized benefits of using income tax depreciation (MACRS) rather than financial depreciation for the computation of income tax liabilities. The total depreciation deduction is the same irrespective of the method of depreciation, however the timing of the deduction gives rise to a difference between tax and book accounting. The calculation compares the present worth of the tax deductions using the prescribed MACRS tables to the present worth of the tax deductions using straight line depreciation.

For ease of explanation, all the assets in the demonstration are assumed to have a MACRS life of seven years, which is the most common MACRS class of depreciable property. The applicable MACRS depreciation percentage is applied to the amount of depreciable assets to calculate the tax depreciation expense for each year. The financial depreciation expenses are assumed to be on the straight line basis. The present worth of the depreciation deduction is calculated for each method and the ratio of the present values of tax to book is the amount of the adjustment. It is possible for the adjustment to be less than one, which would occur if the remaining life of the assets were much shorter than the lives prescribed by the Internal Revenue Code.

The 'J' factor calculation is not used in the perpetual life CEA calculation if the unit consists primarily of used assets. If the unit consists primarily of used assets, the adjustment would not be material.

Taxable Percent and Average Business Inventory

Line No.	[a] Reference	[b] Description	[c] Amount
1		Historical Cost of Property in Service	$ 200,000,000
2		Plus Historical Cost of Nontaxable Property	$ 5,000,000
3			
4	*L1 + L2*	Total Taxable and Nontaxable Property	$ 205,000,000
5			
6	*L1 / L4*	**Taxable Percent**	**97.56%**
7			
8			
9			
10			
11			
12			
13			
14			
15			
16			
17		Beginning Year Business Inventory	*$ 55,000*
18			
19		Year End Business Inventory	*65,000*
20			
21	*L17 + L19*	Total Beginning and Year End Inventory	$ 120,000
22			
23	*L21 / 2*	**Average Business Inventory**	**$ 60,000**
24			
25			
26			
27			
28			
29			
30			
31			
32			
33			
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Average Business Inventory and Taxable Percent

Taxable Percent

The value of nontaxable assets (primarily licensed vehicles) is removed from the income approaches through the use of a taxable percent.

The taxable percent will be identical for all three models, but will be applied to the specific model's capitalized earning value. This taxable percent is calculated by dividing the historical cost of taxable property by the total of both taxable and non-taxable property. The taxable percent is then multiplied by the Capitalized Earning Ability (CEA) to extract the non-taxable value from the CEA approach. The result is an estimated CEA, which excludes the value of nontaxable property.

(Taxable Property at cost / Total Property at cost) = taxable percent

where Taxable Property includes only taxable property, Total Property includes taxable and non-taxable property.

Average Business Inventory

Business inventories are eligible for exemption from taxation under Section 129 of the Revenue and Taxation Code. The amount of business inventory reflected in the CEA is the average inventory during the year at book cost. Therefore, the amount deducted from the CEA is the average inventory amount, rather than the balance at the lien date.

The property statements request the average quantity and amount of inventory, at book costs, and on hand during the calendar year. These figures may be calculated by averaging the twelve month-end balances or the average may be calculated by averaging the beginning and ending year balances.

Possessory Interest

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Possessory Interest		$ 262,450
2		Rent or Franchise Payment		
3				
4	*Note*	Basic Capitalization Rate	13.28%	
~~5~~	~~*Note*~~	~~Ad Valorem Tax Rate~~	~~1.05%~~	
6	*Note*	Income Tax Component	8.12%	
7	$\frac{i}{(1+i)^{n}-1}$	Amount to Accumulate $1	2.42%	
8				
9	*L4 thru L7*	Total Capitalization Rate		23.82%
~~9~~	~~*L4 thru L7*~~	~~Total Capitalization Rate~~		~~24.67%~~
10				
11	*L2 / L9*	**Possessory Interest**		**$ 1,101,900**
~~11~~	~~*L2 / L9*~~	~~**Possessory Interest**~~		~~**$ 1,063,832**~~
12				
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38		Note: The basic capitalization rate and income tax component used in the computations		
39		above should match those used in the calculation of the capitalized earnings ability (CEA)		
40		value indicators.		

Possessory Interest

Possessory Interest

A possessory interest is an interest in real property that exists as a result of the possession of, or a right to possess or occupy land and/or improvements unaccompanied by ownership of a fee simple or life estate in the property. A taxable possessory interest normally exists whenever a utility has exclusive right to possess tax-exempt, publicly-owned property. The utility benefits from the possession of this property right, and it is taxed for the value of the benefits it receives.[45]

A taxable possessory interest value is added to the value indicator because it is a real property right that is not generally represented on the balance sheet of the assessees' accounting records.[46]

A taxable possessory interest can be valued using any of three primary appraisal approaches: cost, income, or comparative sales. For mass appraisal, the most common approach used is the income approach because data regarding economic or market rents and franchise fee payments are readily available.

When valuing a possessory interest by the income approach, the present worth of the economic net income attributed to the property for the permitted use is discounted for the estimated term of possession. The discount rate is comprised of a basic capitalization rate, an income tax component, ~~an ad valorem property tax rate,~~ and the amount to accumulate $1 (calculated at the basic capitalization rate ~~plus the ad valorem tax rate~~). The formula is:

$$ER / (Y_o + ITC + \sout{ETR +} AAO)$$

where ER is the economic or market rent, Y_o is the basic capitalization rate, ITC is the income tax component, ~~ETR is the effective ad valorem tax rate,~~ and AAO is the amount to accumulate $1.

Some companies, such as gas or electric transmission and distribution utilities that are rate base regulated, are allowed to recover the property taxes paid on possessory interests as a component of the rates charged to customers. When calculating the CEA for properties subject to rate base regulation, the property taxes on the possessory interest should be removed from anticipated operating revenue to avoid including the recovery of the possessory interest property taxes as an element of value in the CEA.

[45] Revenue and Taxation Code sections 107, 107.1, 107.4; Property Tax Rules 20-22, 27, 28.
[46] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach.

Present Worth of Land Reversion

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Future California Land Value		$ 500,000
2				
3		*Basic Capitalization Rate*	13.28%	
4		*Ad Valorem Tax Rate*	1.05%	
5				
6	*L3 + L4*	Total Rate	14.33%	
7				
8	*L20*	Present Worth of 1, 14.33%, REL: 15 Years		0.1342
9				
10	*L1 * L8*	**Present Worth of Land Reversion**		**$ 67,100**

$$1/(1+Y)^{REL} = \quad 1/(1+.1433)^{15} = \quad 0.1342$$

The present worth of a reversion where Y is the basic capitalization rate plus a property tax component and REL is the remaining economic life.

Present Worth of Land Reversion

The land reversion is assumed to be a single lump-sum benefit that a utility receives at the termination of the composite remaining economic life (REL). At the end of the income projection period or composite REL for limited life models, land value exists and is referred to as the Land Reversion. The value of the reversion is added to the capitalized income. The Perpetual Model assumes a continuous income into perpetuity. Therefore, no land reversion is required.

To value the single lump-sum payment, the expected payment is multiplied by the compound interest factor for the present value of $1 at the selected discount rate. A component for ad valorem property taxes is added to the discount rate. Thus:

PV = Land Value times PW$1 (@ Y_o + ETR)

where PV is the present value of the payment; PW$1 is the present worth (or value) of $1; Y_o is the basic capitalization rate; and ETR is the effective ad valorem tax rate.[47]

[47] Assessor's Handbook 502, Chapter 4, page 102.

Construction Work in Progress Additive and Future Use Property

Line No.	[a] Reference	[b] Description	[c] Amount
1		Reproduction Cost New (RCN) of Depreciable Plant in Service	$ 100,000,000
2			
3		Total Construction Work in Progress (CWIP)	2,000,000
4			
5	*L1 * 1.5%*	*Less Estimate of Replacement CWIP*	*1,500,000*
6			
7	*L3 - L5 [Note]*	**Construction Work in Progress Additive**	**$ 500,000**
8			
9			
10			
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17			
18		Total Future Use Property	$ 200,000
19		Amount in Rate Base	100,000
20			
21	*L18 - L 19*	**Future Use Property**	$ 100,000
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39		Note: Reported new CWIP should be used as the additive. If this is not available, the calculation	
40		above should be used to estimate new CWIP	

Construction Work In Progress Additive and Future Use Property

Construction Work In Progress Additive

The CEA of a company normally reflects the construction work in progress (CWIP) required to maintain replacement of the existing facilities. However, CWIP for new plant is normally not reflected in the income stream, because the new CWIP has not had the opportunity to contribute to the earnings. An additive to the CEA is therefore required.

A state assessee reports to the Board the amount of new CWIP. If such information is not available, the assessee should report an estimate of its new CWIP. If this is not available an estimate of the new CWIP is calculated by the appraiser. This additive is calculated as follows:

Total CWIP - (RCN * 1.5%)

where Total CWIP is the total CWIP including replacement CWIP and new CWIP recorded as of the lien date, and RCN is the replacement or reproduction cost new of depreciable plant in service prior to depreciation.

Future Use Property

Future Use Property consists of property that is owned and held for future use in service by a utility. Future Use Property includes assets acquired but never used by a utility or assets previously held by the utility in service, but retired from such service and held pending its reuse in the future.[48] If this property is included in the rate base and the earning ability of this property is reflected in the revenue, no additive is necessary. Future Use Property not included in the rate base should be added to the CEA.

[48] Federal Energy Regulatory Commission Statutes & Regulations - Accounting and Reporting Requirements for Natural Gas Companies, pages 13,070-13,071.

Net Liquidation Value (NLV) Model

Net Liquidation Value (NLV) does not project the income of an operating unit. This CEA Model projects the net cash flow that could be expected by breaking apart the operating unit and selling the individual assets. This is an appropriate value indicator to use when the subject property has either functional or economic obsolescence to such a degree that it is more profitable to liquidate the assets than to operate the property. Of the properties subject to central assessment, the railroad industry is the only industry group for which a NLV is computed. The NLV is appropriate for those railroad properties that either have no income or such a low income that a purchaser would expect to achieve a higher return by breaking the property up and selling the component parts than by operating the unit as a railroad.

The NLV calculation begins by estimating the net proceeds from the sale of the assets. The amount of the proceeds are then discounted from the anticipated date of sale to the lien date by a discount factor that includes components for the property taxes due during the holding period and the income taxes that would be due upon the sale of the assets.

The proceeds for rolling stock and other personal property are estimated by using the reproduction cost less depreciation of these assets. No discount is allowed because little time is needed to sell these items.

A one year average time period is usually allowed for the dismantling and disposal of the track and track structure. The amount of the proceeds from the sale of the track and track structure is net of the costs required to dismantle and ship the assets and to the location of the sale.

A two-year average time period is usually allowed for the sale of land and structures. This time period would allow for the track to be removed and the land to be exposed to the real estate market. The value of land included in this estimate should be based on sales of adjacent parcels adjusted for the irregular shapes and sizes usually encountered in railroad right-of-way parcels.

Net Liquidation Value Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Estimated Proceeds from Sale of Rolling		
2		Stock and Equipment		$ 500,000
3				
4		Estimated Proceeds from Sale of Track		
5		and Track Structure	$ 1,500,000	
6				
7	CEA11, L4	Discount factor - one year	0.7869	
8				
9	L5 * L7	Present Value of Track and Track Structure		1,180,350
10				
11		Estimated Proceeds from Sale of Land	$ 4,000,000	
12				
13	CEA11, L4	Discount factor - two years	0.6308	
14				
15	L11 * L13	Present Value of Land		2,523,200
16				
17	L2+L9+L15	**Total Net Liquidation Value**		**$ 4,203,550**
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Discount Factors

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Year	1	2
2		Proof:		
3		Sales Price	$ 10,000,000	$ 10,000,000
4		**Discount Factor**	**0.7869**	**0.6308**
5				
6	*L3 * L4*	Present Worth	$ 7,868,639	$ 6,308,313
7				
8	*L3 - L6*	Gain On Sale	$ 2,131,361	$ 3,691,687
9				
10	*L8 * L25*	Income Taxes	$ 868,444	$ 1,504,215
11				
12	*L3 - L10*	Proceeds After Tax	$ 9,131,556	$ 8,495,785
13	*L27*	Present Worth of $ 1 @ Capitalization Rate + Ad Valorem Rate	0.8617	0.7425
14				
15	*L12*L13*	Present Value	$ 7,868,639	$ 6,308,313
16				
17	*L6 - L15*	Difference	0	0
18				
19				
20				
21				
22		Property Tax Rate	1.05%	1.05%
23		Maximum Federal Tax Rate	35.00%	35.00%
24		State Income Tax Rate	8.84%	8.84%
25	*L23+L24-(L23*L24)*	Combined Income Tax Rate	40.75%	40.75%
26		Capitalization Rate	15.00%	15.00%
27	*1/(1+.15+.0105)^n*	Present Worth of $ 1 @ Capitalization Rate + Ad Valorem Rate	0.8617	0.7425
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Discount Factors

The calculation of the discount factors in the net liquidation value reflects the proper discount that a prospective purchaser would apply to the cash flows generated by liquidating the assets. These factors compute the discount a purchaser would apply to each annual cash flow that would allow the purchaser to achieve the required rate of return after paying the property taxes due during the holding period and the income taxes due upon the sale. Each factor is obtained by using a computer program that generates the factor using an iterative process to solve an equation. The proof shows that the factor calculated for the one year period and the two year period will provide the required rate of return to a purchaser of the assets on an after tax basis.

The capitalization rate used is higher than the rates recommended in operating railroad valuations to reflect more risk because of intermittent cash flows. No debt component to the capitalization rate is used because of the difficulty in obtaining financing for a salvage venture.

A projected sales price of $10,000,000 is used to demonstrate the factor calculation. This sales price is the sales price at some future point of time. The iterative process generates a factor to solve the equation for the present value of the future cash flow.

Income taxes due on the sale of the assets are then estimated by multiplying the gain on the sale by the corporate tax rate. The after-tax proceeds are then discounted by the present worth of a single payment at a rate that includes a component for property taxes to arrive at the present value of the cash flow.

Subtracting the discounted value of the cash flow after income taxes from the present worth generated by the use of the calculated factor demonstrates that the factors used provide for the income taxes a purchaser would incur on a sale and provide the required after-tax return on the original investment.

Sales Model

Overview

The sales model is a variation of the traditional comparative sales model. It differs from the latter because it uses the sales price of the subject directly, usually without comparing it to the sales of other comparable properties.

The comparative sales model is based on the principle of substitution.[49] It assumes that the market value of a property will approximate the sales price of competitive substitutes. It is the preferred method of valuation when reliable market data are available.[50]

In the case of the sale of a utility, it is frequently difficult to apply the traditional comparative sales approach. There are several reasons contributing to the difficulty in using the traditional comparative sales approach:

- The uniqueness of each utility company.
- The size and the monopolistic/ oligopolistic nature of utility companies making them less subject to sales.[51]
- The difficulty of obtaining information from different utility companies to make comparison feasible.

Even though there is weakness in a sales model utilizing few or no comparable sales, the model is a valid indicator of market value. The sale of a utility company is usually an arms-length transaction between a knowledgeable buyer and a knowledgeable seller. Extensive analyses generally are made by both parties with counsel from the best financial experts. Use of the Sales Model in this manner is consistent with the Revenues and Taxation Code Section 110(b) and the Board of Equalization Rule 2(b).

[49] Principle of Substitution: A reasonable purchaser will not pay more for a property than the cost of a substitution that can provide similar utility.
[50] California Code of Regulations, Public Revenue, Title 18 - Property Tax Rule 4, the Comparative Sales Approach to Value.
[51] Sales are more frequent with resellers in the telecommunications industry. In 1997, electric deregulation in California prompted the sale of many electric generation plants. It may be possible to apply the comparative sales approach to such sales.

Sales Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*S1*	Sales Price		$ 25,130,000,000
2				
3		*Less Market Value of Deductible Assets:*		
4	*S2*	*Deductible Assets*	*$ 860,000,000*	
5	*S3*	*Nonutility Operations*	*3,769,500,000*	
6	*S4*	*Intangible Assets*	*450,000,000*	
7		*Total Market Value of Deductible Assets*		*5,079,500,000*
8				
9	*L1-L7*	Sales Price of Utility Operations Net of Deductible Assets		$ 20,050,500,000
10	*S5*	California Utility Allocation Factor		0.9412
11	*L9*L10*	California Utility Value Net of Deductible Assets		$ 18,871,058,824
12	*S5*	Unitary Allocation Factor		0.9500
13				
14	*L11*L12*	Taxable Sales Value		$ 17,927,505,882
15				
16		*Plus Additions to Taxable Sales Value:*		
17	S6	*Possessory Interest*	*$ 1,101,900*	
~~17~~	~~S6~~	~~*Possessory Interest*~~	~~*$ 1,063,800*~~	
18	S6	*Noncapitalized Leased Property*	*5,366,059*	
19	*L17+L18*	*Total Additions to Taxable Sales Value*		*6,467,959*
~~19~~	~~*L17+L18*~~	~~*Total Additions to Taxable Sales Value*~~		~~*6,429,859*~~
20				
21	*L14+L19*	**Sales Indicator**		**$ 17,933,973,842**
~~21~~	~~*L14+L19*~~	~~**Sales Indicator**~~		~~**$ 17,933,935,742**~~
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Sales Price

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Equity Sales Price:		
2		Cash or Cash Equivalent	$ -	
3		Stock Price on Date of Transaction	12,740,000,000	
4		Legal and Professional Fee	480,000,000	
5		Other Costs	320,000,000	
6	*L2 thru L5*	Total Equity Sales Price		$ 13,540,000,000
7				
8		Liabilities Assumed:		
9		Current Liabilities	$ 500,000,000	
10		Long Term Debt	10,000,000,000	
11		Deferred Credits and Other L/T Liabilities	1,090,000,000	
12	*L9 + L10 + L11*	Total Liabilities Assumed		11,590,000,000
13				
14	*L6 + L12*	**Sales Price**		**$ 25,130,000,000**
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Sales Price

The sales price in the case of a utility company is made up of two parts: the sales price paid for the equity interest and the fair market value of any liabilities assumed.

The sales price paid for the equity interest can be in the form of cash, stocks, exchange of stocks, or other non-cash items. Stocks and non-cash items should be converted to cash equivalents by estimating their fair market value on the date of sale. Additionally, any legal or professional fees, or incidental costs incurred related to the sale should be added to the sales price.

The liabilities assumed include current liabilities, long term debts, deferred credits and other long term liabilities. They should be estimated at market value as of the date of sale.

The data needed for Schedule S1 can generally be obtained by examining trade journals and financial reports to shareholders and regulatory agencies.

Deductible Assets

Line No.	[a] Reference	[b] Description	[c] Amount
1		Deductible Assets:	
2		Cash and Cash Equivalents	$ 1,000,000
3		Investments	20,000,000
4		Accounts Receivable	600,000,000
5		Notes Receivable	20,000,000
6		Prepaid Expenses	500,000
7		Misc. Deferred Charges	37,500,000
8		Inventories	105,000,000
9		Leashold Improvement	50,000,000
10		Property in Federal Enclaves	12,000,000
11		Licensed Motor Vehicles	14,000,000
12			
13	*L2 thru L11*	**Total Deductible Assets**	**$ 860,000,000**
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Deductible Assets

The Revenue and Taxation Code has provisions for assets exempt from property taxation. The related provisions are Section 212 (a) and (b) and Section 219.

Section 212 states that:
(a) Notes, debentures, shares of capital stock, solvent credits, bonds, deeds of trust, mortgages, and any interest in that property are exempt from taxation.
(b) Money kept on hand to be used in the ordinary and regular course of a trade, profession, or business is exempt from taxation.

Section 219 states that:
For the 1980-81 fiscal year and fiscal years thereafter, business inventories are exempt from taxation and the assessor shall not assess business inventories.

Based on the above provisions, a company's cash, cash equivalents, investments, receivables, prepaid expenses, and inventories are all exempt and should be removed from the sales price for property tax purposes.

In addition, Revenue and Taxation Code Section 10758 (fee in lieu of ad valorem taxes) provides that vehicles subject to license fees imposed by the Department of Motor Vehicles (DMV) are not to be assessed again by other assessment agencies because property taxes have been paid as part of the fee paid to DMV.

Other deductible property includes leasehold improvements (if the improvements are taxed to the lessor) and property in federal enclaves.

Data needed for the deductible assets can be obtained from financial statements and reports to shareholders or regulatory agencies.

Nonutility Operations

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*S1*	Sales Price		$ 25,130,000,000
2				
3		Consolidated Income from Operations before		
4		Interest, Extraordinary Items and Income Taxes	$ 5,000,000,000	
5				
6		Income from Nonutility Operations before		
7		Interest, Extraordinary Items and Income Taxes	750,000,000	
8				
9	*L7 / L4*	% of Nonutility Income to Consolidated Income		15.00%
10				
11	L1 * L9	**Nonutility Operations**		**$ 3,769,500,000**
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Nonutility Operations

If a company has both utility and nonutility operations, the value of nonutility operations should be removed from the sales price to arrive at a value indicator for the utility operations only.

The method illustrated in Schedule S3 to calculate the percentage of nonutility income to consolidated income is referred to as the "Income Influence Method" by the Western States Association of Tax Administrators. Applying the percentage so derived to the sales price leads to the amount of the sales price attributed to nonutility operations.

Usually, the consolidated income from all operations and incomes from various segments can be obtained by examining the company's financial statements or reports filed with regulatory agencies.

Intangible Assets

Line No.	[a] Reference	[b] Description	[c] Amount
1		Intangible Assets:	
2		Organization	$ 2,000,000
3		Goodwill	448,000,000
4			
5	*L2 + L3*	**Total Intangible Assets**	**$ 450,000,000**
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42		Note: Appendx I addresses exempt intangibles.	

California Utility Allocation Factor and Unitary Allocation Factor

Line No.	[a] Reference	[b] Description	[c] Amount
1		Income from System Utility Operation before	
2		Interest, Extraordinary Items, and Income Taxes	$ 4,250,000,000
3			
4		Income from California Utility Operations before	
5		Interest, Extrordinary Items and Income Taxes	4,000,000,000
6			
7			
8	*L5 / L2*	**California Utility Allocation Factor**	**0.9412**
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18			
19		Income from California Utility Operations before	
20		Interest, Extrordinary Items and Income Taxes	$ 4,000,000,000
21			
22		Income from California Unitary Operations before	
23		Interest, Extrordinary Items and Income Taxes	3,800,000,000
24			
25			
26	*L23 / L20*	**Unitary Allocation Factor**	**0.9500**
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California Utility Allocation Factor and Unitary Allocation Factor

California Utility Allocation Factor

When a company operates both within and outside California, only the properties within California are subject to property tax. A factor is used to allocate the value between properties within California and outside California.

The allocation factor is obtained by dividing income from California utility operation before interest, extraordinary items and income taxes by consolidated income before interest, extraordinary items and income taxes. Both data can be obtained by examining the company's financial statements to shareholders and regulatory agencies.

Unitary Allocation Factor

Revenue and Taxation Code Section 723 states that the Board may use the principle of unit valuation to value all the properties of an assessee that are operated as a unit in the primary function of the assessee. When so valued, the properties are known as "unitary properties". The properties of an assessee not valued through the use of the principle of unit valuation are known as "nonunitary properties". Based on this provision, the Board uses the principle of unit valuation when appraising public utilities and railroads.

To separate unitary property from nonunitary property, a factor or ratio derived from unitary income (or nonunitary income) to the total income is used. The income can be obtained by examining a company's financial statements, reports filed with the regulatory agencies, or property tax statements.

Possessory Interest and Noncapitalized Leased Property

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1		Possessory Interest		
2		Rent or Franchise Payment		$ 262,450
3				
4	*Note*	Basic Capitalization Rate	13.280%	
~~5~~	~~*Note*~~	~~Ad Valorem Tax Rate~~	~~1.050%~~	
6	*Note*	Income Tax Component	8.120%	
7	$\frac{i}{(1+i)^{n}-1}$	Amount to Amortize $1	2.419%	
8	*L4 thru L7*	Total Capitalization Rate		23.819%
~~8~~	~~*L4 thru L7*~~	~~Total Capitalization Rate~~		~~24.670%~~
9				
10	*L2 / L8*	**Possessory Interest**		**$ 1,101,900**
~~10~~	~~*L2 / L8*~~	~~**Possessory Interest**~~		~~**$ 1,063,800**~~
11				
12				
13				
14				
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19				
20		Minimum Annual Lease Payments for 10 years		$ 1,000,000
21				
22		Basic Capitalization Rate	13.28%	
23	$\frac{i}{(1+i)^{n}-1}$	Amount to Accumulate $1 - 10 years	5.36%	
24				
25	*L22 + L23*	Total Capitalization Rate		18.64%
26				
27				
28	*L20 / L25*	**Noncapitalized Leased Property**		**$ 5,366,059**
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40		Note: The basic capitalization rate and income tax component used in the computations		
41		above should match those used in the calculation of the capitalized earnings ability (CEA)		
42		value indicators.		

Possessory Interest and Noncapitalized Leased Property

Possessory Interest

A possessory interest is an interest in real property that exists as a result of the possession of, or a right to possess or occupy land and/or improvements unaccompanied by ownership of a fee simple or life estate in the property. A taxable possessory interest normally exists whenever a utility has exclusive right to possess tax-exempt, publicly-owned property. The utility benefits from the possession of this property right, and it is taxed for the value of the benefits it receives.[52]

A taxable possessory interest value is added to the value indicator because it is a real property right that is not generally represented on the balance sheet of the assessee's accounting records.[53]

A taxable possessory interest can be valued using any of three primary appraisal approaches: cost, income, or comparative sales. For mass appraisal, the most common approach used is the income approach because data regarding economic or market rents and franchise fee payments are readily available.

When valuing a possessory interest by the income approach, the present worth of the economic net income attributed to the property for the permitted use is discounted for the estimated term of possession. The discount rate is comprised of a basic capitalization rate, an income tax component, ~~an ad valorem property tax rate,~~ and the amount to accumulate $1 (calculated at the basic capitalization rate ~~plus the ad valorem tax rate~~). The formula is:

$$ER / (Y_o + ITC + \sout{ETR +} AAO)$$

where ER the economic or market rent, Y_o the basic capitalization rate, ITC is the income tax component, ~~ETR is the effective ad valorem tax rate,~~ and AAO is the amount to accumulate $1.

Noncapitalized Leased Property

Noncapitalized leased property is an additive to the unitary value indicator(s) because leased properties are not recorded on the utility's accounting records except for capitalized leased properties that should be reported in the same manner as property purchased.[54]

In the sales approach, the present value of the future minimum lease payments should be added as an adjustment to the sales price. Although these assets are typically not included in the sale, they are included in the unitary property so an adjustment is required.

[52] Revenue and Taxation Code sections 107, 107.1, 107.4; Property Tax Rules 20-22, 27, 28.
[53] Western States Association of Tax Administrators, Appraisal Handbook, Section II - Cost Approach.
[54] The appraiser should ascertain whether the recorded cost represent market value.

Pipeline Rate Base Model

Overview

The income from common carrier pipeline property is regulated by law. The Federal Energy Regulatory Commission (FERC) allows the use of net depreciated Trended Original Cost (TOC) as a rate base. Under the TOC rate base model, the pipeline investment is segregated into debt and equity segments based on the capital structure of the pipeline. The debt portion is valued at historical cost less depreciation, while the costs represented by the equity segment are trended by inflation factors and depreciation is recalculated based on the trended cost.

If the pipeline operates in more than one state, the TOC rate base is allocated to California by the use of an interstate allocation formula. Adjustments are then made for other taxable property not included in the rate base (e.g., noncarrier property or construction work in progress). In addition, property included in the rate base, but outside the assessment jurisdiction of the Board of Equalization (e.g., locally-assessed property) must be removed.

Pipeline Rate Base Model

Line No.	[a] Reference	[b] Description	[c] Amount	[d] Amount
1	*RB1*	System Rate Base		$1,500,000,000
2	*RB2*	Interstate Allocation Factor		0.21
3	*L1*L2*	California Rate Base		$ 315,000,000
4	*RB3*	State-Assessed Plant and Equipment Factor		0.63
5	*L3*L4*	California State-Assessed Rate Base		$ 198,450,000
6				
7	*RB1*	*Plus: Construction Work in Progress (CWIP) - State Assessed*	*$ 100,000,000*	
8	*RB3*	*Other Adjustments*	*100,000,000*	
9		*Total Additions to Rate Base Value*		*200,000,000*
10				
11	*L5+L9*	**Rate Base Value Indicator**		**$ 398,450,000**
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Adjusted System Rate Base and Construction Work in Progress

Adjusted System Rate Base

System Rate Base is an estimate of assessee's system regulatory rate base. System means that the rate base reflects all pipeline operations, not just those located within California. For property tax reporting purposes, deferred income tax liabilities shall be separately identified and not included in the reported system rate base.

The FERC and the CPUC require the accumulated DIT to be deducted from the rate base. The pipeline operator cannot earn a return on the portion of the rate base represented by DIT because the regulators do not allow a return on investment made with funds provided by deferring the payment of income taxes. However, the operator is allowed to recover the cost of these investments and the rates reflect the recovery of such costs through depreciation. ~~For this reason, the entire amount of DIT should not be deducted from the rate base indicator. The DIT balance should be adjusted to reflect the economic impairment and that amount should be deducted~~.

In this example, the Adjusted System Rate Base is $1,500,000,000 ($1,550,000,000 less $50,000,000). The assessee reported a system rate base of $1,550,000,000 and a deferred income tax balance of $~~100~~50,000,000. ~~A deduction of 50% of the deferred income tax balance was allowed for valuation purposes.~~

Construction Work in Progress - State Assessed

Regulatory authorities do not include construction work in progress in the rate base. However, CWIP is included in the unitary value indicator because it has value and is taxable for property tax purposes.

Interstate Allocation Factor

Line No.	[a] Reference		[b] Description	[c] Amount	[d] Amount
1		I.	Property Investment:		
2			System Historical Cost	$ 2,000,000,000	
3			*Remove:*		
4			*Adjustments for assets purchased over H.C. (Acct. 166)*	*(5,000,000)*	
5			*CWIP*	*(300,000,000)*	
6	*L2-L4-L5*		Total System Cost for Allocation		$ 1,695,000,000
7					
8			*California Historical Cost w/o CWIP and M&S:*		
9			*State-Assessed*	*$ 250,000,000*	
10			*County-Assessed*	*150,000,000*	
11	*L9+L10*		Total California Cost for Allocation		$ 400,000,000
12					
13	*L11/L6*		California Factor for Allocation		0.24
14					
15					
16		II.	Barrel Miles:	California	System
17			*Total Barrel Miles*	*6,000,000,000*	*60,000,000,000*
18					
19	*L17CA/L17SYS*		Barrel Miles Factor For Allocation		0.10
20					
21					
22		III.	Terminal - Originating & Terminating Barrels:	California	System
23			*Barrels Received*	*54,000,000*	*456,000,000*
24			*Barrels Delivered*	*54,000,000*	*455,000,000*
25					
26	*L23 + L24*		*Total Originating and Terminating Barrels*	*108,000,000*	*911,000,000*
27					
28	*L26CA/L26SYS*		Originating & Terminating Barrels Factor For Allocation		0.12
29					
30					
31					
32					

Line No.				California Percentage	Weighting Factor	Weighted Factor
33		IV.	Weighted Basis			
34	*L13 * 75%*		*Historical Cost*	*0.24*	*0.75*	*0.18*
35	*L19 * 20%*		*Barrel Miles*	*0.10*	*0.20*	*0.02*
36	*L28 * 5%*		*Originating & Terminating Barrels*	*0.12*	*0.05*	*0.01*
37						
38			**California Interstate Allocation Factor**			***0.21***
39						
40						
41						
42						

RB2

California Interstate Allocation Factor

The California interstate allocation factor applies only to interstate pipeline systems that report system rate base numbers. The purpose of this factor is to allocate a portion of the system value to each state. The allocation should reasonably reflect the relative value of assets that have situs in each state.

In calculating the interstate allocation factor staff relies upon the Western States Association of Tax Administrators (WSATA) formula. The WSATA formula uses both property and use factors to allocate the property of interstate pipelines among the respective assessment jurisdictions.

- Property - The property factor is intended to reflect the contribution of various physical assets of the operating system and to identify the distribution of these assets throughout the system. The property factor is based on undepreciated property costs in each state.
- Use - The use factor allocates system value based on the proportion of physical activity within each state to the activity of the entire system. Use factors for a pipeline include barrel-miles to measure relative pipeline usage and originating-and-terminating-barrels to measure relative terminal activity.

Once the property and use factors are identified, ratios are developed by dividing the California property and use factors by the property and use factors of the total system. A 75% weight is applied to the property ratio, a 20% weight is applied to the use factor of barrel-miles, and a 5% weight is applied to the use factor of originating-and-terminating-barrels.[1]

[1] Western States Association of Tax Administrators Appraisal Handbook - Allocation of Unitary Property page 116.

State-Assessed Plant and Equipment Factor and Other Adjustments

Line No.	[a] Reference	[b] Description	[c] Amount
1		State-Assessed Plant and Equipment	$ 250,000,000
2		County-Assessed Plant and Equipment	146,825,397
3			
4	*L1 + L2*	Total California Plant and Equipment	$ 396,825,397
5			
6	*L1/L4*	**State Assessed Plant and Equipment Factor**	**0.63**
7			
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17		Noncarrier Property	$ 50,000,000
18		Property not included in the Rate Base	50,000,000
19			
20	*L17 + L18*	**Total Other Adjustments**	**$ 100,000,000**
21			
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State Assessed Plant and Equipment Factor and Construction Work in Progress

State Assessed Plant and Equipment Factor

The reported rate base includes property that is not assessed by the Board of Equalization. This locally assessed property should be removed from the rate base value indicator.

A factor is used to remove the portion of property that is locally assessed. This factor is calculated by dividing the cost of state-assessed plant and equipment by the total California plant and equipment. The resulting factor is then applied to the California rate base to arrive at the California State Assessed rate base.

Other Adjustments

Other adjustments may be required in order to include nonregulated property or other property not included in the rate base, such as pipeline segments carrying product to military bases. The assessee is required to report such information in detail so that the Valuation Division can make the necessary adjustments to the value indicator.

Appendix I: Exempt Intangibles

Revenue and Taxation Code Section 110 defines "full cash value" and states in 110 (d) (e) & (f) that:

> (d) Except as provided in subdivision (e), for purposes of determining the "full cash value" or "fair market value" of any taxable property, all of the following shall apply:
> (1) The value of intangible assets and rights relating to the going concern value of a business using taxable property shall not enhance or be reflected in the value of the taxable property.
> (2) If the principal of unit valuation is used to value properties that are operated as a unit and the unit includes intangible assets and rights, then the fair market value of the taxable property contained within the unit shall be determined by removing from the value of the unit the fair market value of the intangible assets and rights contained within the unit.
> (3) The exclusive nature of a concession, franchise, or similar agreement, whether de jure or de facto, is an intangible asset that shall not enhance the value of taxable property, including real property.
> (e) Taxable property may be assessed and valued by assuming the presence of intangible assets or rights necessary to put the taxable property to beneficial or productive use.
> (f) For purposes of determining the "full cash value" or "fair market value" of real property, intangible attributes of real property shall be reflected in the value of the real property. These intangible attributes of real property include zoning, location, and other such attributes that relate directly to the real property involved

The above is the basis for the inclusion or exclusion of intangibles in the derivation of staff's value indicators. Any adjustments made to the indicators for intangibles are to be based on sound appraisal methods. [2] In the CEA approaches, the staff removes intangible value(s) by imputing an income to the intangible item(s) and deducts the imputed income from the income to be capitalized in accordance with Property Tax Rule 8 (e). The direct deduction of reported, recorded, or staff estimated intangible values from the value indicator are used to remove intangible values included in other approaches.

The appraisal treatment of intangible assets is more fully discussed in Assessors' Handbook 502 starting at page 150.

[2] The appraiser should insure that the indicator(s) includes the value of the intangible before making an adjustment.

Appendix II: Selected Property Tax Rules *(as of March 2000)*

Rule 1. **GENERAL APPLICATION.**

References: Sections 110, 110.1, 401, Revenue and Taxation Code; *Carlson* v. *Assessment Appeals Board No. 1* (1985) 167 Cal. App. 3d 1004; *Dennis* v. *County of Santa Clara* (1989) 215 Cal. App. 3d 1019.

The rules in this subchapter govern assessors when assessing, county boards of equalization and assessment appeals boards when equalizing, and the State Board of Equalization, including all divisions of the property tax department.

History: Adopted June 21, 1967, effective July 23, 1967.
Amended July 27, 1982, effective December 30, 1982.

Rule 2. **THE VALUE CONCEPT.**

References: Article 2, Chapter 3, Part 2, Division 1, Revenue and Taxation Code.
Sections 110, 110.1, 401, Revenue and Taxation Code.

(a) In addition to the meaning ascribed to them in the Revenue and Taxation Code, the words "full value," "full cash value," "cash value," "actual value," and "fair market value" mean the price at which a property, if exposed for sale in the open market with a reasonable time for the seller to find a purchaser, would transfer for cash or its equivalent under prevailing market conditions between parties who have knowledge of the uses to which the property may be put, both seeking to maximize their gains and neither being in a position to take advantage of the exigencies of the other.

When applied to real property, the words "full value", "full cash value", "cash value", "actual value" and "fair market value" mean the prices at which the unencumbered or unrestricted fee simple interest in the real property (subject to any legally enforceable governmental restrictions) would transfer for cash or its equivalent under the conditions set forth in the preceding sentence.

(b) When valuing real property (as described in paragraph (a)) as the result of a change in ownership (as defined in Revenue and Taxation Code, Section 60, et seq.) for consideration, it shall be rebuttably presumed that the consideration valued in money, whether paid in money or otherwise, is the full cash value of the property. The presumption shall shift the burden of proving value by a preponderance of the evidence to the party seeking to overcome the presumption. The presumption may be rebutted by evidence that the full cash value of the property is significantly more or less than the total cash equivalent of the consideration paid for the property. A significant deviation means a deviation of more than 5% of the total consideration.

(c) The presumption provided in this section shall not apply to:

(1) The transfer of any taxable possessory interest.

(2) The transfer of real property when the consideration is in whole, or in part, in the form of ownership interests in a legal entity (e.g., shares of stock) or the change in ownership occurs as the result of the acquisition of ownership interests in a legal entity.

(3) The transfer of real property when the information prescribed in the change in ownership statement is not timely provided.

(d) If a single transaction results in a change in ownership of more than one parcel of real property, the purchase price shall be allocated among those parcels and other assets, if any, transferred based on the relative fair market value of each.

History: Adopted June 21, 1967, effective July 23, 1967.
Amended December 17, 1975, effective January 25, 1976.
Amended October 9, 1984, effective September 20, 1985.
Amended July 24, 1991, effective September 25, 1991.

Rule 3. VALUE APPROACHES.

References: Article 2, Chapter 3, Part 2, Division 1, Revenue and Taxation Code.
Sections 110, 401, Revenue and Taxation Code.

In estimating value as defined in section 2, the assessor shall consider one or more of the following, as may be appropriate for the property being appraised:

(a) The price or prices at which the property and comparable properties have recently sold (the comparative sales approach).

(b) The prices at which fractional interests in the property or comparable properties have recently sold, and the extent to which such prices would have been increased had there been no prior claims on the assets (the stock and debt approach).

(c) The cost of replacing reproducible property with new property of similar utility, or of reproducing the property at its present site and at present price levels, less the extent to which the value has been reduced by depreciation, including both physical deterioration and obsolescence (the replacement or reproduction cost approach).

(d) If the income from the property is regulated by law and the regulatory agency uses historical cost or historical cost less depreciation as a rate base, the amount invested in the property or the amount invested less depreciation computed by the method employed by the regulatory agency (the historical cost approach).

(e) The amount that investors would be willing to pay for the right to receive the income that the property would be expected to yield, with the risks attendant upon its receipt (the income approach).

History: Adopted June 21, 1967, effective July 23, 1967.

Rule 4. THE COMPARATIVE SALES APPROACH TO VALUE.

References: Sections 110, 110.1, 110.5, 401, Revenue and Taxation Code.
Article XIII A, Sections 1, 2, California Constitution.

When reliable market data are available with respect to a given real property, the preferred method of valuation is by reference to sales prices. In using sales prices of the appraisal subject or of comparable properties to value a property, the assessor shall:

(a) Convert a noncash sale price to its cash equivalent by estimating the value in cash of any tangible or intangible property other than cash which the seller accepted in full or partial payment for the subject property and adding it to the cash portion of the sale price and by deducting from the nominal sale price any amount which the seller paid in lieu of interest to a lender who supplied the grantee with part or all of the purchase money.

(b) When appraising an unencumbered-fee interest, (1) convert the sale price of a property encumbered with a debt to which the property remained subject to its unencumbered-fee price

equivalent by adding to the sale price of the seller's equity the price for which it is estimated that such debt could have been sold under value-indicative conditions at the time the sale price was negotiated and (2) convert the sale price of a property encumbered with a lease to which the property remained subject to its unencumbered-fee price equivalent by deducting from the sale price of the seller's equity the amount by which it is estimated that the lease enhanced that price or adding to the price of the seller's equity the amount by which it is estimated that the lease depressed that price.

(c) Convert a sale to the valuation date of the subject property by adjusting it for any change in price level of this type of property that has occurred between the time the sale price was negotiated and the valuation date of the subject property.

(d) Make such allowances as he deems appropriate for differences between a comparable property at the time of sale and the subject property on the valuation date, in physical attributes of the properties, location of the properties, legally enforceable restrictions on the properties' use, and the income and amenities which the properties are expected to produce. When the appraisal subject is land and the comparable property is land of smaller dimensions, and it is assumed that the subject property would be divided into comparable smaller parcels by a purchaser, the assessor shall allow for the cost of subdivision, for the area required for streets and alleys, for selling expenses, for normal profit, and for interest charges during the period over which it is anticipated that the smaller properties will be marketed.

History: Adopted June 21, 1967, effective July 23, 1967.
Amended July 27, 1982, effective December 30, 1982.

Rule 6. THE REPRODUCTION AND REPLACEMENT COST APPROACHES TO VALUE.

Reference: Sections 110, 401, Revenue and Taxation Code.

(a) The reproduction or replacement cost approach to value is used in conjunction with other value approaches and is preferred when neither reliable sales data (including sales of fractional interests) nor reliable income data are available and when the income from the property is not so regulated as to make such cost irrelevant. It is particularly appropriate for construction work in progress and for other property that has experienced relatively little physical deterioration, is not misplaced, is neither over- nor underimproved, and is not affected by other forms of depreciation or obsolescence.

(b) The reproduction cost of a reproducible property other than inventory (for which see section 10 of this chapter) may be estimated either by (1) adjusting the property's original cost for price level changes and for abnormalities, if any, or (2) applying current prices to the property's labor and material components, with appropriate additions for entrepreneurial services, interest on borrowed or owner-supplied funds, and other costs typically incurred in bringing the property to a finished state (or to a lesser state if unfinished on the lien date). Estimates made under (2) above may be made by using square-foot, cubic-foot, or other unit costs; a summation of the in-place costs of all components; a quantity survey of all material, labor, and other cost elements; or a combination of these methods.

(c) The original cost of reproducible property shall be adjusted, in the aggregate or by groups, for price level changes since original construction by multiplying the cost incurred in a given year by an appropriate price index factor. When detailed investment records are unavailable for earlier years or when only a small percentage of the total investment is involved, the investments in such years may be lumped and factored to present price levels by means of an index number that represents the assessor's best judgment of the weighted average price change. If the property was not new when acquired by its present owner and its original cost is unknown, its acquisition cost may be substituted for original cost in the foregoing calculations.

(d) The replacement cost of a reproducible property other than inventory may be estimated as indicated in (b)(2) of this section by applying current prices to the labor and material components of a substitute property capable of yielding the same services and amenities, with appropriate additions as specified in subsection (b)(2).

(e) Reproduction or replacement cost shall be reduced by the amount that such cost is estimated to exceed the current value of the reproducible property by reason of physical deterioration, misplacement, over- or underimprovement, and other forms of depreciation or obsolescence. The percentage that the remainder represents of the reproduction or replacement cost is the property's percent good.

(f) When the allowance made pursuant to paragraph (e) exceeds the amount included in the depreciation tables used by the assessor, the reasons therefor shall be noted in the appraisal record for the property and the amount thereof shall be ascertainable from the record.

(g) This rule shall first be observed in assessing property for the 1968-69 fiscal year.

History: Adopted September 1, 1967, effective October 7, 1967.
Amended February 16, 1970, effective March 26, 1970.
Amended February 18, 1971, effective March 24, 1971.
Amended February 16, 1977, effective February 18, 1977.

Rule 8. THE INCOME APPROACH TO VALUE.

Reference: Sections 110, 401, Revenue and Taxation Code.

(a) The income approach to value is used in conjunction with other approaches when the property under appraisal is typically purchased in anticipation of a money income and either has an established income stream or can be attributed a real or hypothetical income stream by comparison with other properties. It is the preferred approach for the appraisal of land when reliable sales data for comparable properties are not available. It is the preferred approach for the appraisal of improved real properties and personal properties when reliable sales data are not available and the cost approaches are unreliable because the reproducible property has suffered considerable physical depreciation, functional obsolescence or economic obsolescence, is a substantial over- or underimprovement, is misplaced, or is subject to legal restrictions on income that are unrelated to cost.

(b) Using the income approach, an appraiser values an income property by computing the present worth of a future income stream. This present worth depends upon the size, shape, and duration of the estimated stream and upon the capitalization rate at which future income is discounted to its present worth. Ideally, the income stream is divided into annual segments and the present worth of the total income stream is the algebraic sum (negative items subtracted from positive items) of the present worths of the several segments. In practical application, the stream is usually either

(1) divided into longer segments, such as the estimated economic life of the improvements and all time thereafter or the estimated economic life of the improvements and the year in which the improvements are scrapped and the land is sold, or
(2) divided horizontally by projecting a perpetual income for land and an income for the economic life of the improvements, or
(3) projected as a level perpetual flow.

(c) The amount to be capitalized is the net return which a reasonably well informed owner and reasonably well informed buyers may anticipate on the valuation date that the taxable property existing on that date will yield under prudent management and subject to such legally enforceable

restrictions as such persons may foresee as of that date. Net return, in this context, is the difference between gross return and gross outgo. Gross return means any money or money's worth which the property will yield over and above vacancy and collection losses, including ordinary income, return of capital, and the total proceeds from sales of all or part of the property. Gross outgo means any outlay of money or money's worth, including current expenses and capital expenditures (or annual allowances therefor) required to develop and maintain the estimated income. Gross outgo does not include amortization, depreciation, or depletion charges, debt retirement, interest on funds invested in the property, or rents and royalties payable by the assessee for use of the property. Property taxes, corporation net income taxes, and corporation franchise taxes measured by net income are also excluded from gross outgo.

(d) In valuing property encumbered by a lease, the net income to be capitalized is the amount the property would yield were it not so encumbered, whether this amount exceeds or falls short of the contract rent and whether the lessor or the lessee has agreed to pay the property tax.

(e) Recently derived income and recently negotiated rents or royalties (plus any taxes paid on the property by the lessee) of the subject property and comparable properties should be used in estimating the future income if, in the opinion of the appraiser, they are reasonably indicative of the income the property will produce in its highest and best use under prudent management. Income derived from rental of properties is preferred to income derived from their operation since income derived from operation is the more likely to be influenced by managerial skills and may arise in part from nontaxable property or other sources. When income from operating a property is used, sufficient income shall be excluded to provide a return on working capital and other nontaxable operating assets and to compensate unpaid or underpaid management.

(f) When the appraised value is to be used to arrive at an assessed value, the capitalization rate is to include a property tax component, where applicable, equal to the estimated future tax rate for the area times the assessment ratio.

(g) The capitalization rate may be developed by either of two means:

(1) By comparing the net incomes that could reasonably have been anticipated from recently sold comparable properties with their sales prices, adjusted, if necessary, to cash equivalents (the market-derived rate). This method of deriving a capitalization rate is preferred when the required sales prices and incomes are available. When the comparable properties have similar capital gains prospects, the derived rate already includes a capital gain (or loss) allowance and the income to be capitalized should not include such a gain (or loss) at the terminus of the income estimate.

(2) By deriving a weighted average of the capitalization rates for debt and for equity capital appropriate to the California money markets (the band-of-investment method) and adding increments for expenses that are excluded from outgo because they are based on the value that is being sought or the income that is being capitalized. The appraiser shall weight the rates for debt and equity capital by the respective amounts of such capital he deems most likely to be employed by prospective purchasers.

(h) Income may be capitalized by the use of gross income, gross rent, or gross production multipliers derived by comparing sales prices of closely comparable properties (adjusted, if necessary, to cash equivalents) with their gross incomes, gross rents, or gross production.

(i) The provisions of this rule are not applicable to lands defined as open-space lands by Chapter 1711, Statutes of 1967, nor are they applicable in all respects to possessory interests.

History: Adopted December 12, 1967, effective January 18, 1968.
Amended December 15, 1976, effective January 21, 1977.
Amended September 27, 1977, effective November 25, 1977.
Amended July 27, 1982, effective December 30, 1982.

Rule 20. Taxable Possessory Interests.

Reference: Section 107, Revenue and Taxation Code

(a) POSSESSORY INTERESTS. "Possessory interests" are interests in real property that exist as a result of:

(1) A possession of real property that is independent, durable, and exclusive of rights held by others in the real property, and that provides a private benefit to the possessor, except when coupled with ownership of a fee simple or life estate in the real property in the same person; or
(2) A right to the possession of real property, or a claim to a right to the possession of real property, that is independent, durable, and exclusive of rights held by others in the real property, and that provides a private benefit to the possessor, except when coupled with ownership of a fee simple or life estate in the real property in the same person; or
(3) Taxable improvements on tax-exempt land.

(b) TAXABLE POSSESSORY INTERESTS. "Taxable possessory interests" are possessory interests in publicly-owned real property. Excluded from the meaning of "taxable possessory interests", however, are any possessory interests in real property located within an area to which the United States has exclusive jurisdiction concerning taxation. Such areas are commonly referred to as federal enclaves.

(c) DEFINITIONS. For purposes of this regulation:

(1) "Real property" is defined in section 104 of the Revenue and Taxation Code and includes public waters such as tidelands and navigable waters and waterways.
(2) "Possession" of real property means actual physical occupation. "Possession" requires more than incidental benefit from the public property, but requires actual physical occupation of the property pursuant to rights not granted to the general public; thus, the use of property such as hallways, common areas, and access roads at airports, stadiums, convention centers, or other public facilities by customers or employees of those who may lease other public property at the public facility of which they have exclusive use does not constitute "possession" of those hallways, common areas, or access roads by the lessee of the public property.
(3) A "right," or a "claim to a right," to the possession of real property means the right, or claim to a right, to actual physical occupation of real property. For purposes of this subdivision, a right, or a claim to a right, to the possession of real property may exist as a result of the possessor having or claiming to have: (i) a leasehold estate, an easement, a profit a prendre, or any other legal or equitable interest in real property of less than fee simple or life estate, regardless of how the interest may be identified in a deed, lease, or other document; or (ii) a use permit or agreement, such as a federal grazing permit, a permit to use a berth at a harbor, or a county use permit authorizing professional rafting outfitters to commercially operate on a river, that creates a legal or equitable interest in real property of less than fee simple or life estate.
(4) "Possessor" means the party or parties who hold the possessory interest, and any successors or assigns to such party or parties.
(5) "Independent" means a possession, or a right or claim to possession, if the possession or operation of the real property is sufficiently autonomous to constitute more than a mere agency. To be "sufficiently autonomous" to constitute more than a mere agency, the possessor must have the right and ability to exercise significant authority and control over the management or operation of the real property, separate and apart from the policies, statutes, ordinances, rules, and regulations of the public owner of the real property. For example, the control of an airport runway or taxiway by the Federal Aviation Administration (FAA) or another government agency or its agent is so complete that it precludes the airlines from exercising sufficient authority and control over the management or operation of the runways or taxiway and does not constitute sufficient "independence" to support a possessory interest.
(6) "Durable" means for a determinable period with a reasonable certainty that the possession of the real property by the possessor, or the possessor's right or claim with respect to the possession of the real property, will continue for that period.

(7) "Exclusive of rights held by others in the real property" means the enjoyment of an exclusive use of real property, or a right or claim to the enjoyment of an exclusive use together with the ability to exclude from possession by means of legal process others who may interfere with that enjoyment.

(A) For purposes of this subdivision, "exclusive uses" include the following types of uses of real property, as well as rights and claims to such types of uses of real property:

(1) The sole possession, occupancy, or use of real property,

(2) The possession, occupancy, or use of real property by co-tenants or co-owners as to leaseholds, easements, profits a prendre, or any other legal or equitable interests in real property of less than fee simple or life estate, where the uses constitute but a single use jointly enjoyed.

(3) The concurrent use of real property, not amounting to co-tenancy or co-ownership under subdivision (A)(2) above, by a person who has a primary or prevailing right to use the real property and/or to have its designees use the real property. For example, a public marina leases boat slips with a lease provision that allows the marina to rent a leased boat slip to a short-term user if the primary lessee is away; subject to the primary lessee's right to exclude the short-term user on the primary lessee's return. Under these facts, the primary lessee has a primary and prevailing right to use the leased boat slip. For purposes of this subdivision, concurrent use of real property demonstrating a primary or prevailing right also includes alternating uses of the same real property by more than one party, such as the case when certain premises are used by a professional basketball team on certain days of each week while a professional hockey team uses the same premises on certain other days.

(4) Concurrent uses of real property, not amounting to co-tenancy or co-ownership under subdivision (A)(2) above, by persons making qualitatively different uses of the real property. For purposes of this subdivision, qualitatively different uses of real property include: (i) those by persons making different kinds of uses of the same real property, such as the case when one person is developing mineral resources on real property while others are concurrently enjoying recreational uses on the same real property; and (ii) those where different persons have the right to concurrently enter onto and take different things from the same real property.

(5) Concurrent uses of real property, not amounting to co-tenancy or co-ownership under subdivision (A)(2) above, by persons engaged in qualitatively similar uses that diminish the quantity or quality of the real property. For purposes of this subdivision, uses that diminish the quantity and/or quality of the real property include: (i) grazing cattle; (ii) mining: (iii) the extraction of oil or gas; and (iv) the extraction of geothermal energy.

(6) Concurrent uses of real property, not amounting to co-tenancy or co-ownership under subdivision (A)(2) above, by persons engaged in qualitatively similar uses that do not diminish the quantity or quality of the real property, provided that the number of concurrent use grants is restricted. For purposes of this subdivision: "concurrent use grants" includes grants, permits, deeds, agreements, and other documents providing rights to the concurrent use of real property; and the number of concurrent use grants is "restricted" when the number of concurrent use grants is restricted either by law or pursuant to the policies or management decisions of the public owner of the real property or other public agency.

Example 1: Commercial rafting outfitters have a county use permit to commercially operate on a river. While any private recreational user may raft on the river without limitation or regulation, only approximately 80 commercial rafting outfitters are presently allowed to operate under permit on the river. The commercial rafting outfitters' use of the river is exclusive for purposes of this regulation since the number of commercial use permits issued by the county to commercial rafting outfitters is restricted, regardless of whether or not the commercial rafting outfitters' use of the river diminishes its quantity or quality.

Example 2: X operates a shuttle van service, picking up passengers at their homes and other locations, and transporting them to the airport. When the shuttle van reaches the airport, it utilizes the public street which surrounds the airport to drop passengers off at the various terminals at the airport. The

street around the airport is available to all licensed drivers, for commercial and noncommercial uses. Neither the traffic laws, nor the policies or management decisions of the public owner of the airport facility restrict the number of users of the public street. In addition, under the assumed facts of this hypothetical, X's use of the public street surrounding the airport does not diminish the quantity or quality of the real property.
Given that (i) the shuttle vans using the public street are making qualitatively similar uses of that real property; (ii) there are no facts indicating that the quality or quantity of the real property is being diminished; and (iii) the number of users of the real property is not restricted, X's right to use the public street surrounding the airport is not exclusive, and X does not have a possessory interest in the public street surrounding the airport.

(B) A use of real property, or a right or claim to a use of real property, that does not contain one of the elements in subdivisions (A)(1) to (6) above, inclusive, shall be rebuttably presumed to be nonexclusive.

(C) In no event shall the presence of occasional trespassers or occasional interfering uses be sufficient in and of itself to make nonexclusive a use, or a right or claim to a use, that is otherwise exclusive for purposes of this regulation.

(8) "Private benefit" means that the possessor has the opportunity to make a profit, or to use or be provided an amenity, or to pursue a private purpose in conjunction with its use of the possessory interest. The use should be of some private or economic benefit to the possessor that is not shared by the general public. The fact that a possession of real property is not for a business or commercial purpose or that the possessor is a non-profit corporation does not preclude the possessor from being found to have received a "private benefit" from that possession.

History: Adopted January 22, 1998, effective May 6, 1998

Rule 21. **TAXABLE POSSESSORY INTERESTS-VALUATION ~~Possessory Interest Definitions.~~**

Reference: Sections 107, 107.1, Revenue and Taxation Code.
Section 15606, subdivision (c), Government Code.

~~The following definitions govern the construction of these words in the rules pertaining to possessory interests.~~

~~**(a)** "Contract rent" means payments in money or in kind for the right to use real property as required by the terms of the possessory interest agreement. It includes royalty payments and other rights to share in production, the value that the public owner is expected to realize from improvements erected at the expense of the possessor which will remain when the possessory interest terminates, and any other form of compensation paid or payable for the right to occupy the property. It does not, however, include payments for services such as utilities and janitorial labor or for the use of property not subject to the possessory interest.~~

~~**(b)** "Economic rent" means the amount that would be paid in money or kind for the right to use real property if (1) the contract rent were currently negotiated under the conditions which exist in a free and competitive market and (2) the fee owner paid property taxes on the value of the fee.~~

~~**(c)** "Extended or renewed" means the lengthening of the term of possession of an agreement by mutual consent or by the exercise of an option by either party to the agreement.~~

~~**(d)** "Created" includes (1) the addition of land or improvements not previously subject to the agreement and (2) the addition of valuable permitted uses not previously permitted.~~

(a) Definitions. For the purposes of this regulation:

(1) "Real property" is defined in rule 20(c)(1).

(2) "Possession" is defined in rule 20(c)(2).

(3) A "right" to the possession of real property includes a "claim to a right" to the possession of real property within the meaning of rule 20(c)(3).

(4) "Possessor" is defined in rule 20(c)(4).

(5) The "term of possession" of a taxable possessory interest means the term of possession for valuation purposes.

(6) The "stated term of possession" for a taxable possessory interest as of a specific date is the remaining period of possession as of that date as specified in the lease, agreement, deed, conveyance, permit, or other authorization or instrument that created, extended, or renewed the taxable possessory interest, including any option or options to renew or extend the specified period of possession if it is reasonable to assume that the option or options will be exercised.

(7) "Contract rent" means any compensation or payments, in cash or its equivalent, that are required to be paid or provided by a possessor under an authorization or instrument that creates a taxable possessory interest for the rights in real property provided by the taxable possessory interest.

(8) "Economic rent" means the estimated amount that would be paid by the possessor, on the valuation date in cash or its equivalent, for the rights in real property provided by the taxable possessory interest if (i) the rights to possession were offered in an open and competitive market and (ii) the public owner's interest in the property were not exempt or immune from taxation. Economic rent does not include payments by the possessor to the public owner that are not paid as consideration for rights in real property, such as payments for the rental of personal property, for the provision of security services, and for advertising and promotional services.

(9) "Creation" means the creation of a taxable possessory interest. Creation includes (i) an initial grant or other conveyance of a taxable possessory interest; (ii) a subsequent grant or other conveyance of additional land or improvements to a preexisting taxable possessory interest; or (iii) a subsequent grant or other conveyance of additional valuable property rights or uses to a preexisting taxable possessory interest.

(10) "Extension or renewal" means the lengthening of the period of possession of a taxable possessory interest, such as by the exercise of an option to extend or to renew a lease or permit.

(b) Rights to be Valued. Except as provided in subsection (f) or specifically provided otherwise by law, the rights to be valued in a taxable possessory interest are all rights in real property held by the possessor.

(1)The fair market value of a taxable possessory interest is not diminished by any obligation of the possessor to pay rent or to retire debt secured by the taxable possessory interest. In other words, the fair market value of a taxable possessory interest is the fair market value of the fee simple absolute interest reduced only by the value of the property rights, if any, granted by the public owner to other persons and by the value of the property rights retained by the public owner (excluding the public owner's right to receive rent).

(2) Examples of rights in real property that may be granted or retained by the public owner include the following: (i) the right to take possession of the property upon the termination

of the taxable possessory interest due to the occurrence of an event such as the expiration of the contract term, a breach of agreement, or the happening of a condition that terminates the possessor's right to possession; (ii) the right to put the property to a higher and better use or otherwise restrict the possessor's use of the property; (iii) the right to terminate possession upon notice; (iv) the right to approve a sublessee or assignee; (v) the right to approve a loan secured by the taxable possessory interest; and (vi) the right to allow other possessors to use the property.

(c) Standard of Value. Assessors shall value a taxable possessory interest consistent with the requirements of subsections (a), (d), (e), and (f) of section 110 of the Revenue and Taxation Code. A taxable possessory interest subject to article XIII A of the California Constitution shall also be valued consistent with the requirements of section 110.1 of the Revenue and Taxation Code.

(d) Term of Possession for Valuation Purposes

(1) The term of possession for valuation purposes shall be the reasonably anticipated term of possession. The stated term of possession shall be deemed the reasonably anticipated term of possession unless it is demonstrated by clear and convincing evidence that the public owner and the private possessor have reached a mutual understanding or agreement, whether or not in writing, such that the reasonably anticipated term of possession is shorter or longer than the stated term of possession. If so demonstrated, the term of possession shall be the stated term of possession as modified by the terms of the mutual understanding or agreement.

(2) If there is no stated term of possession, the reasonably anticipated term of possession shall be demonstrated by the intent of the public owner and the private possessor, and by the intent of similarly situated parties, using criteria such as the following:

(A) The sale price of the subject taxable possessory interest and sales prices of comparable taxable possessory interests.

(B) The rules, policies, and customs of the public owner and of similarly situated public owners.

(C) The customs and practices of the private possessor and of similarly situated private possessors.

(D) The history of the relationship of the public owner and the private possessor and the histories of the relationships of similarly situated public owners and private possessors.

(E) The actions of the parties to the subject taxable possessory interest, including any amounts invested in improvements by the public owner or the private possessor.

(3) For the purposes of this regulation, a taxable possessory interest that runs from month to month, a taxable possessory interest without fixed term, or a taxable possessory interest of otherwise unspecified duration shall be deemed to be a taxable possessory interest with no stated term of possession.

(e) Valuation of Post-De Luz Taxable Possessory Interests. Except as specifically provided otherwise by law, and excluding a taxable possessory interest involving the production of gas, petroleum, or other hydrocarbons, the value of a taxable possessory interest created, extended, or renewed after December 24, 1955 (i.e., a "Post-De Luz" taxable possessory interest) may be estimated using one or more of the following methods, as appropriate for the taxable possessory interest being valued.

(1) Comparative Sales Approach to Value. In the comparative sales approach, a taxable possessory interest is valued using the sale price of the subject taxable possessory interest or

sales prices of comparable taxable possessory interests, provided such interests shall have sold under the conditions of fair market value described in subsection (a) of section 110. A taxable possessory interest may be valued by the direct comparison method or the indirect comparison method.

(A) Direct Comparison Method

~~1.~~In the direct comparison method, the appraiser shall add the following to the sale price of the subject taxable possessory interest, or to the sale price of a comparable taxable possessory interest, to derive an indicator of the fair market value of the subject taxable possessory interest: (i) the present value on the sale date of any unpaid future contract rent for the term of possession; (ii) the fair market value on the sale date of any debt assumed by the buyer of the taxable possessory interest; and (iii) the present value on the sale date of any future costs that the buyer is contractually obligated to pay for the right of possession (e.g., the cost of site restoration at the end of the term of possession) less the present value on the sale date of any future benefits in addition to the right of possession or use that the buyer is contractually entitled to receive (e.g., the salvage value of, or reimbursement value for, improvements existing at the end of the term of possession). The unpaid future contract rent in (i) above shall be reduced by any expense necessary to maintain the income from the taxable possessory interest, including any element of "gross outgo" as defined in subsection (c) of rule 8.

~~2.~~When valuing a taxable possessory interest by comparison with the sales of other taxable possessory interests, the other taxable possessory interests shall be located sufficiently near the subject taxable possessory interest and shall be sufficiently alike in respect to character, size, situation, usability, zoning or other enforceable government restrictions on use (unless rebutted pursuant to subdivision (c) of section 402.1 of the Revenue and Taxation Code), and restrictions on possession or use contained in the legal authorization or instrument that created extended or renewed the taxable possessory interest to make it clear that the comparable taxable possessory interests and the subject taxable possessory interest are comparable in value and that the cash equivalent price realized for the comparable taxable possessory interests may fairly be considered as shedding light on the value of the subject taxable possessory interest. The comparable sales also shall be sufficiently near in time to the valuation date of the subject taxable possessory interest. "Near in time to the valuation date" does not include any sale more than 90 days after the valuation ~~lien~~ date.

(B) Indirect Comparison Method.

In the indirect comparison method, a taxable possessory interest is valued by (i) estimating the fair market value on the valuation date of the possessor's rights in real property in the taxable possessory interest as if owned in perpetuity (i.e., the value of the fee simple absolute interest in such rights) using sales of fee simple absolute interests in properties that are comparable to the subject property as prescribed in section 402.5 of the Revenue and Taxation Code and whose highest and best use corresponds to, or is comparable with, the permitted use of the subject taxable possessory interest; and (ii) reducing this value by both the present value of those property rights for the period subsequent to the term of possession (i.e., the value of the fee simple absolute interest in such rights at the end of the term of possession) and the present value of all other rights of fee simple absolute ownership, if any, that are not provided to the possessor.

(2) Cost Approach to Value. In the cost approach, a taxable possessory interest is valued by (i) adding the estimated replacement cost new less depreciation of improvements that meet the requirements of the possessor's permitted use to the estimated value of the taxable possessory interest in land; and (ii) reducing this amount by the estimated present value of the improvements that shall revert to or be retained by the public owner at the end of the term of

possession.

(A) The replacement cost new less depreciation of the improvements may be estimated as prescribed in subsections (d) and (e) of rule 6. The estimated value of the taxable possessory interest in land may be estimated using the comparative sales approach (direct or indirect method) or the income approach (direct or indirect method), as prescribed in subsections (e)(1) and (e)(3).

(B) If a possessor's property use is limited to specified time periods (e.g., certain hours of the day or certain days of the week) or is shared with other possessors, the value determined by the cost approach shall be reasonably allocated to each possessor in a manner that reflects each possessor's proportionate value of the right to possession.

(3) Income Approach to Value. In the income approach, a taxable possessory interest is valued by discounting the future net income that the interest in real property is capable of producing. A taxable possessory interest may be valued using the direct income method or the indirect income method.

(A) Direct Income Method. In the direct income method, a taxable possessory interest is valued by capitalizing the future net income that the taxable possessory interest is capable of producing under typical, prudent management for the term of possession.

(B) Indirect Income Method. In the indirect income method, a taxable possessory interest is valued by (i) estimating the fair market value of the possessor's rights on the valuation date as if owned in perpetuity (i.e., the value of the fee simple absolute interest in such rights) using the income approach to value as prescribed in rule 8; and (ii) reducing this value by the present value of the those rights for the period subsequent to the term of possession (i.e., the present value of the value of the fee simple interest in such rights at the end of the term of possession).

(C) Income to be Capitalized. The income to be capitalized in the valuation of a taxable possessory interest is the "net return" (as defined in subsection (c) of rule 8) attributable to the taxable possessory interest. The income to be capitalized may be based on either (i) the estimated economic rent for the subject taxable possessory interest or (ii) if the estimated economic rent is unreliable or unavailable, the estimated net operating income of a typical, prudent operator of the property subject to the taxable possessory interest. Rental income is preferable to operating income (i.e., income from operating a business) because operating income may be influenced by managerial skills and may derive, in part, from nontaxable property. The income to be capitalized must be attributable to the rights in real property in the subject taxable possessory interest and must reflect the restrictions on use inherent in the subject taxable possessory interest.

~~1.~~Economic rent

a. The economic rent of the subject taxable possessory interest may be estimated by reference to (i) the contract rent for the subject taxable possessory interest; (ii) contract rents for comparable taxable possessory interests; (iii) contract rents for comparable fee simple absolute interests in real property; or (iv) contract rents for other comparable interests in real property. All such contract rents shall have been negotiated in an open and competitive market involving real property reasonably comparable to the subject taxable possessory interest in terms of physical attributes, location, legally enforceable restrictions on the property's use, term of possession, and risk of cancellation of the taxable possessory interest by public owner. In addition, the contract rents shall have been negotiated sufficiently near in time to the valuation date as to shed light on the economic rent of the

subject taxable possessory interest.

b. When using the contract rent of a taxable possessory interest as an indicator of the economic rent, the assessor shall add to the contract rent (i) an estimate of the amount, if any, by which the contract rent has been reduced because improvements have been constructed at the possessor's expense that will revert to the public owner at the end of the term of possession; and (ii) an estimate of the amount, if any, by which the contract rent has been reduced because the possessor will bear the cost of restoring the real property to its original condition on reversion to the public owner, including the cost of removing improvements (less any estimated salvage value of, or reimbursement value for, the improvements), or the cost of any similar obligation.

c. To arrive at the income to be capitalized, any expense necessary to maintain the income from the subject taxable possessory interest, including any element of "gross outgo" as defined in subsection (c) of rule 8, whether paid by the public owner or the possessor, must be deducted from the estimated economic rent if the expense will be paid out of the estimated economic rent.

~~2.~~ Net Operating Income

a. Net operating income is gross operating income less allowed expenses. Gross operating income, allowed expenses, and net operating income are defined herein consistent with "gross return," "gross outgo," and "net return," respectively, in subsection (c) of rule 8.

b. When valuing a taxable possessory interest using operating income, allowed expenses include the following: cost of goods sold (if applicable), typical operating expenses, typical management expense, an allowance for a return on working capital, and an allowance for a return on the value of any nontaxable property that contributes to the gross operating income. Typical operating expenses may include expenses for the rental of personal property, for the provision of security services, and for advertising and promotional services, provided such expenses are necessary for the production of the gross income. Typical operating expenses and typical management expense include expenses that an owner/operator typically would bear to maintain the property and to continue the production of income from the property but are borne by the public owner in the case of the subject taxable possessory interest.

c. Allowed expenses do not include the following: amortization, depreciation, depletion charges, debt retirement, interest on funds invested in the taxable possessory interest, the contract rent for the taxable possessory interest, property taxes on the taxable possessory interest, income taxes, or state franchise taxes measured by income.

(D) Capitalization Rate. Subsection (g) of rule 8 provides that a capitalization rate may be developed by either comparing the anticipated net incomes of recently sold comparable properties with their sales prices, or by deriving a weighted average of the capitalization rates (rates of return) for debt and equity capital appropriate to California money markets. In accordance with rule 8, the capitalization rate used in the valuation of a taxable possessory interest may be developed by (i) comparing the anticipated net incomes from comparable taxable possessory interests with their sales prices stated in cash or its equivalent and adjusted as described in subsection (e)(1)(A); (ii) comparing the anticipated net incomes of comparable fee simple absolute interests in real property with their sales prices stated in cash or its equivalent, provided the comparable fee properties are not expected to produce significantly higher net incomes subsequent to

the subject taxable possessory interest's term of possession than during it; or (iii) by deriving a weighted average of the capitalization rates for debt and equity capital appropriate for the subject taxable possessory interest, weighting the separate rates of debt and equity by the relative amounts of debt and equity capital expected to be used by a typical purchaser of the subject taxable possessory interest. Consistent with subsection (f) of rule 8, the capitalization rate shall contain a component for property taxes where applicable.

(f) Valuation of Pre-De Luz Taxable Possessory Interests. Except as specifically provided otherwise by law, and excluding a taxable possessory interest involving the production of gas, petroleum, or other hydrocarbons, the value of a taxable possessory interest created prior to December 24, 1955, and not since renewed or extended (i.e., a "Pre-De Luz" taxable possessory interest) is the excess of the fair market value on the valuation date of the taxable possessory interest over the present value of unpaid future contract rent for the unexpired term of possession (i.e., for the term of possession). This value may be estimated using one or more of the following methods, as appropriate for the taxable possessory interest being valued.

(1) Comparative Sales Approach to Value. A Pre-De Luz taxable possessory interest may be valued by the comparative sales approach using the direct comparison method or the indirect comparison method, as described in subsection (e)(1), but with the following modifications:

(A) Direct Comparison Method. In the direct comparison method, the present value of the unpaid future contract rent is not added to the sale price of the taxable possessory interest.

(B) Indirect Comparison Method. In the indirect comparison method, the value of the possessor's rights as if owned in fee is reduced by the present value of the unpaid future contract rent of the taxable possessory interest, as well as by the value of those property rights for the period subsequent to the term of possession.

(2) Cost Approach to Value. A Pre-De Luz taxable possessory interest may be valued by the cost approach as described in subsection (e)(2), but the present value of any unpaid future contract rent of the taxable possessory interest in land for the term of possession is also deducted.

(3) Income Approach to Value. A Pre-De Luz taxable possessory interest may be valued by the income approach using the direct income method or the indirect income method, as described in subsection (e)(3), but with the following modifications:

(A) Direct Income Method. In the direct income method, the net income to be capitalized is reduced by the unpaid future contract rent for the term of possession, as well as by allowed expenses.

(B) Indirect Income Method. In the indirect income method, the present value of the unpaid future contract rent for the term of possession is deducted from the value of the fee interest, as well as the deduction of the present value of the property rights for the period subsequent to the term of possession.

History: Adopted January 6, 1971, effective February 18, 1971.
Amended December 17, 1975, effective January 25, 1976.
Amended January 22, 1998, effective May 6, 1998.
Amended March 27, Amended March 27, 2002, effective July 11, 2002. Amended to provide for the valuation of taxable possessory interests and to include provisions of former rules 23, 24, 25, and 26, which were repealed.

Rule 22. **CONTINUITY OF POSSESSORY INTERESTS.**

Reference: Sections 107, 107.1, 107.4, Revenue and Taxation Code.

(a) The continuity of possession or exclusive use necessary to establish a possessory interest will vary according to the location and character of the property. The continuity of use necessary for finding a possessory interest to exist is satisfied when the possessor of the property uses it to substantially the same extent as would an owner engaged in the same activity.

(b) Standards for determining the existence of taxable possessory interests based on continuity are:

(1) Actual or constructive possession or exclusive use of property on the lien date for the current year.

(2) Recurrent possession or exclusive use, whether or not the period extends through the lien date, when there is a history on the lien date of recurring use by the present or former possessors making a similar use of the property.

(3) Infrequent actual possession or exclusive use on a recurrent basis when the continuation of the right to possession or exclusive use is conditioned on or evidenced by the possessor having made a contribution to the value of the property by way of investment on or near the property occupied.

History: Adopted January 6, 1971, effective February 18, 1971.

~~**Rule 23.** **WRITTEN AGREEMENTS AS TO TERM OF POSSESSORY INTERESTS.**~~

~~*Reference:* Sections 107, 107.1, 107.4, Revenue and Taxation Code.~~

~~**(a)** When a written instrument creating a possessory interest specifies a period of occupancy which is to exist, the stated period shall be taken as the term of possession for purposes of valuation except as provided in this section. An option period shall be considered part of the stated period if it is reasonable to conclude that the option will be exercised.~~

~~**(b)** Should a period thus determined be in conflict with the reasonably anticipated term of possession by the possessor and any successor to or assignee of the property interest, the reasonably anticipated term of possession, whether shorter or longer, shall be used instead of the stated period. In determining the reasonably anticipated term of possession, the assessor shall be guided by the intent of the public owner and the possessor, as indicated by such evidence as (1) sale prices of the subject or similar possessory interests, (2) the history of the property's use, (3) the policy of the public agency administering the lands, and (4) the actions of the possessor. No reduction or increase of the specified period shall be based on the life expectancy of the possessor if it is reasonably anticipated that possession will continue under his successors or assigns.~~

~~**(c)** When there is no stated term of possession, the term shall be determined in accordance with subsection (b).~~

~~*History:* Adopted January 6, 1971, effective February 18, 1971.~~

~~**Rule 24.** **POSSESSORY INTEREST RIGHTS TO BE VALUED.**~~

Reference: Sections 107, 107.1, 107.4, Revenue and Taxation Code.

Except as otherwise provided in sections 26 and 27 of this title, the taxable value of a possessory interest is the sum of the value of all property rights in land and improvements held by the possessor. This value is not diminished by any obligation to pay rent or to retire debt secured by the possessory interest. Stated in other terms, the taxable value of a possessory interest is the value of the fee simple estate reduced by the value of any rights, except security interests, held by the public owner (other than the right to receive rent) or granted by the public owner to other persons. Examples of rights held by the public owner are:

(a) The right to take possession of the property upon termination of the possessory interest by reason of expiration of the term or the happening of a condition or breach of a limitation contained in the agreement granting possession.

(b) The right to put the property to a higher and better use or otherwise restrict the possessor's use of the property.

(c) The right to terminate possession on notice.

(d) The right to approve a sublessee or assignee.

(e) The right to approve a loan secured by the possessory interest.

History: Adopted January 6, 1971, effective February 18, 1971.

Rule 25. VALUATION OF POST-DE LUZ POSSESSORY INTERESTS.

Reference: Sections 107, 107.1, 107.4, Revenue and Taxation Code.

The value of a taxable possessory interest created, extended, or renewed after December 24, 1955 (other than one for production of gas, petroleum, or other hydrocarbons) may be measured by one or more of the following methods:

(a) The "comparative sales approach," wherein the possessory interest is valued by either direct or indirect comparison as follows:

In the direct comparison method, the subject property is compared with itself on the date of a prior subsequent sale or with similar possessory interests which have been sold on dates prior or subsequent to the date as of which the property is being valued. To the sale price of such an interest there shall be added (1) the present worth of any unpaid future contract rents for the estimated remaining term of possession, (2) the value of any debt (other than the debt for future rents) assumed by the purchaser of the possessory interest, and (3) the present worth of any obligated costs of the purchaser, such as the cost of site restoration at the end of the term, less the present worth of any contractual benefits to the purchaser, such as salvage value of, or reimbursement for, improvements at the end of the term. The interest sold should be reasonably comparable to the possessory interest being valued in location, physical characteristics, term of possession, risk of cancellation, and permitted use.

In the indirect comparison method, the value of the possessor's rights is first measured as if perpetual by comparison with fee interests which have been sold, which have similar locations and physical characteristics, and for which the highest and best use corresponds to or is comparable with the permitted use of the property subject to the possessory interest. This value is reduced by the present worth of those rights for the period subsequent to the estimated term of possession. This method is not well suited to valuation of a short-term possessory interest when the fee interests in the comparable properties are sold at prices that appear to reflect the expectation of higher incomes after the expiration of the possessory interest than during its existence.

(b) The "income approach," wherein the possessory interest is valued either directly by capitalizing all future net income that the possessory interest is capable of generating under typical management during the estimated term of possession, or indirectly by first capitalizing the net income to estimate the value of the possessor's rights as if perpetual and then deducting the present worth of those rights for the period subsequent to the term of the possessory interest.

The direct income method is preferred over the indirect income method when the remaining economic life of wasting assets does not exceed the estimated term of possession or when a constant income stream is projected. The indirect income method is preferred when the remaining economic life of wasting assets exceeds the estimated term of possession.

The net income to be capitalized is either the imputed economic rent, which may be estimated by reference to rentals recently negotiated in a competitive market or, if such evidence is inadequate, by reference to the anticipated gross income of a typical operator of the property subject to the possessory interest, less costs of goods sold and typical management and other operating expenses. When the second of these methods of estimating economic rent is employed, the "other operating expenses" to be deducted do not include amortization, depreciation, depletion charges, debt retirement, interest on funds invested in the possessory interest, the contract rent for the possessory interest, property taxes on the possessory interest, income taxes, or state franchise taxes measured by income.

The imputed economic rent or gross income estimate is to reflect the restrictions on use inherent in the possessory interest.

When using a recently negotiated or percentage contract rent for a possessory interest as an indicator of the economic rent, the appraiser shall:

(1) include in the contract rent his estimate of the amount, if any, by which the cash or share rent has been reduced because the possessor has assumed the cost of improvements that will revert to the public owner on expiration of the possessory interest;

(2) add to the contract rent his estimate of the taxes that will be paid on the possessory interest if the capitalization rate contains a property tax component;

(3) add to the contract rent his estimate of the amount, if any, by which the contract rent was reduced because the possessor has agreed to bear the cost of restoring the property to its original condition when it reverts to the public owner, or the cost of removing improvements and restoring the site to its original condition (less any estimated salvage value), or any similar obligations.

The capitalization rate shall be derived (1) by extraction of a rate from sale prices of comparable possessory interests or from sale prices of fee interests in similar properties that are not expected to yield substantially higher incomes after expiration of the possessory interest being valued than during its existence or (2) by combining weighted components for debt and equity yields as described in section 8, subsection (g)(2) of this chapter. In either case, the capitalization rate shall include a property tax component as required by section 8, subsection (f) of this chapter when the property tax has not been netted out of the rent or other income being capitalized.

(c) The "cost approach," wherein the cost of replacing reproducible property with new property which offers utility that will satisfy the requirements of the possessor's permitted use, less accrued depreciation and less the present worth of the estimated value, if any, of such property at the termination of possession, is added to the value of the restricted right to occupy the land for the limited term derived by the comparative sales or income method.

History: Adopted January 6, 1971, effective February 18, 1971.

Rule 26. VALUATION OF PRE-DE LUZ POSSESSORY INTERESTS.

Reference: Sections 107, 107.1, Revenue and Taxation Code.

The value of a taxable possessory interest created prior to December 25, 1955, and not since extended or renewed (other than one for the production of gas, petroleum, or other hydrocarbons) is the excess of the market value of the possessory interest over the present worth of unpaid future contract rents for the unexpired term of possession. Such value may be measured by one or more of the following methods:

(a) The "comparative sales approach," wherein the possessor's interest is valued either directly or indirectly as previously described in section 25, subsection (a), except that, in the direct comparison method, the present worth of unpaid future contract rents is not added to the sale price of a possessory interest and, in the indirect comparison method, the value of a fee interest is reduced by the present worth of unpaid future contract rents of the possessory interest being appraised as well as by the present worth of the property rights for the period subsequent to the estimated term of possession.

(b) The "income approach," wherein the possessor's interest is valued either directly or indirectly as described in section 25, subsection (b), except that, in the direct method, the unpaid future contract rents, as well as other expenses, are deductible and, in the indirect method, the present worth of unpaid future contract rents, as well as the present worth of the property rights for the period subsequent to the term of the possessory interest, is deductible.

~~**(c) The "cost approach," wherein the possessor's interest is valued as described in section 25, subsection (c), and the present worth of any unpaid future contract rents for the term of the possessory interest is deducted.**~~

History: Adopted January 6, 1971, effective February 18, 1971.

Rule 28. EXAMPLES OF TAXABLE POSSESSORY INTERESTS.

Reference: Sections 107, 107.1, 107.2, 107.3, 107.4, Revenue and Taxation Code.

The following are examples of commonly encountered taxable possessory interests:

(a) The right to explore for, capture, and reduce to possession gas, petroleum, and other hydrocarbons in public lands.

(b) The possession of an employee in housing owned by a public agency, irrespective of whether occupancy of the housing is a condition of employment except when the facility also serves as the employee's work area to which the employer has full access.

(c) The right to cut and remove standing timber on public lands.

(d) The right to graze livestock or raise forage on public lands.

(e) The possession of public property at harbors, factories, airports, golf courses, marinas, recreation areas, parks, and stadiums. Possessory interests may include land subject to the ultimate grant of a United States patent, commercial and industrial sites, and water rights.

History: Adopted January 6, 1971, effective February 18, 1971.

Rule 902. UNITARY PROPERTY VALUE INDICATORS AND STAFF DISCUSSIONS.

Reference: Sections 721, 722, 723, 724, 725, Revenue and Taxation Code.

Each year the Valuation Division shall make capitalization rate studies and develop value indicators applicable to the unitary property of each state assessee. A copy of the appropriate capitalization rate study and a summary of the calculations of the value indicators shall be provided by the Chief, Valuation Division, to the affected assessee on request. The assessee shall be informed that the staff will be available to discuss the data supplied.

History: Adopted January 7, 1976, effective February 8, 1976.

Rule 905. Assessment Electric Generation Facilities

Reference: California Constitution, article XIII, section 19; and section 721, Revenue and Taxation Code.

(a) Commencing with the assessment for the lien date for the 2003 assessment year, an electric generation facility shall be state assessed property for purposes of article XIII, section 19 of the California Constitution if: (1) the facility has a generating capacity of 50 megawatts or more; and (2) is owned or used by a company which is an electrical corporation as defined in subdivisions (a) and (b) of section 218 of the Public Utilities Code; or, the facility is owned or used by a company which is a state assessee for reasons other than its ownership of the electric generation facility or its ownership of pipelines, flumes, canals, ditches, or aqueducts lying within two or more counties.

(b) "Electric generation facility" does not include a qualifying small power production facility or a qualifying cogeneration facility within the meaning of Sections 201 and 210 of Title II of the Public Utility Regulatory Policies Act of 1978 (16 U.S.C. §§796(17), (18) and 824a-3) and the regulations adopted for those sections under that act by the Federal Energy Regulatory Commission (18 C.F.R. 292.101-292.602).

(c) For purposes of this section, "company" means:

(1) A person as defined in Revenue and Taxation Code section 19;

(2) A separate division or other functional unit of a business enterprise which is created and maintained to operate any electric generation facility, where the business enterprise is engaged in a primary business other than generating, transmitting, distributing or selling electricity to the public.

(d) If an electric generation facility is operated by a separate division or other functional unit of a business enterprise, as described in this rule, the business enterprise must maintain accounting and other records sufficient to distinguish the costs and revenues of the separate division or unit from other divisions and units of the business enterprise.

(e) As adopted on September 1, 1999 and effective November 27, 1999, this rule is applicable to define electric generation facilities subject to state assessment to and including December 30, 2002. As amended on November 28, 2001, and filed with the Secretary of State on May 14, 2002, this rule is applicable to define electric generation facilities subject to state assessment as of December 31, 2002 and thereafter.

History: Adopted September 1, 1999, effective November 27, 1999; amended November 28, 2001, effective June 13, 2002.

Glossary

Abnormal Costs - amounts recorded in the property accounting records that are above and beyond what is typically expected in the construction or acquisition of a particular property type. Example: costs incurred to correct construction flaws.

Ad Valorem Tax Component - the part of the total capitalization rate that reflects the property taxes that a hypothetical purchaser would incur upon purchase of the subject property. This component is expressed as a relationship between the expected annual property tax expense and value.

Anticipated Operating Expenses - the amount of future annual expenses anticipated, or expected, from the operation of property by a hypothetical purchaser.

Anticipated Operating Revenues - the amount of future annual revenues anticipated, or expected, from the operation of property by a hypothetical purchaser.

Appraisal Unit - the unit of property that is typically bought and sold in the market.

Band-of-Investment - a method used to derive a capitalization rate in which the appraiser determines the capital structure that a hypothetical purchaser would likely employ and uses the relative percentages of debt and equity to weight the required debt and equity rates of return to develop the basic capitalization rate.

Basic Capitalization Rate - the rate of return on an investment necessary to attract investors. This can be computed by use of the band of investment. This is also known as the return on investment or yield rate, and is prior to any adjustment for capital recapture or taxes.

Book Cost - the amount in dollars of an asset as it is carried in the accounting records of a business. The original cost of an asset.

Capital Structure - the relative percentages of debt and owners' equity that constitute the liability and equity elements of the balance sheet.

Capitalization- any method of converting an income stream into an indicator of value.

Capitalization Rate - a rate used in converting income into an indicator of value. A ratio that expresses a relationship between income and value.

Cash Equivalent - the market value of assets expressed in terms equivalent to cash.

Cash Flow(s) - cash receipts minus disbursements derived from a group of assets for a given period of time.

Comparative Sales Approach - the technique of valuing properties by comparing them with similar properties that have been sold on a specified date. The comparative sales approach requires the sale of a sufficient number of similar properties within a specified period so that their characteristics and sales prices can be compared. It is based on the principle of substitution, which assumes that buyers would not pay more, and sellers would not accept less, for properties that are similar to, or have comparable utilities, to those that are sold in the same time period.

Cost - the expenditure required to develop and construct an improvement or acquire real and personal property.

Cost Worksheet - a worksheet used by the Valuation Division to calculate the cost indicators: Historical Cost Less Depreciation (HCLD) and Reproduction/ Replacement Cost Less Depreciation (RCNLD/ ReplCNLD). It is commonly known as Form V-508.

Debt - an amount owed. The general name for liabilities such as notes, bonds, mortgages that are evidences of amounts owed.

Deferred Charges - miscellaneous long term prepayments. Deferred Charges often is a catchall account for items that do not fit into other asset category and are not material enough individually to constitute a separate category.

Deferred Credits - miscellaneous long term liabilities. Deferred Credits often is a catchall account for long term liabilities that do not fit into other liabilities category and are not material enough individually to constitute a separate category.

Deferred Income Taxes (DIT) - accrued income tax credit or accrued income tax charges arising from the use of different accounting methods for financial reporting and income tax purposes. To conform to regulatory requirements, public utilities generally use straight-line depreciation for financial accounting purposes. However, to minimize income tax liability, accelerated depreciation is generally used. The use of two different depreciation methods creates a tax timing difference known as deferred income taxes.

Depreciation (Appraisal)- a decrease in utility resulting in a loss of the subject property's value. Depreciation can also be expressed as the difference between the replacement / reproduction cost new as of a particular date and the market value at the same date. There are three principal types of depreciation:

- **External (Economic) Obsolescence** - loss in utility and value caused by external negative influences outside the property. The inability of a property to perform the function for which it was originally intended.
- **Functional Obsolescence** - loss in utility and value due to changes in the desirability of the subject property; this may be attributed to changes in taste and style or the result of a poor original design. Functional obsolescence is also curable if the cost to cure is less than the value added by curing this deterioration.
- **Physical deterioration** - loss in utility and value due to physical deterioration in the subject property. Physical deterioration is curable if the cost to cure is less than the value added by curing this deterioration.

Equity - the owners' interest in the assets of a business. It is the residual interest of a business after the claims of non-owners (i.e., debt and other liability holders) are deducted. For a business organized as a corporation, balance sheet equity is typically made up of common stock, preferred stock, and (cumulative) earnings that have not been distributed.

Historical Cost - the total cost of a property when originally acquired, constructed, or first placed into service. Also called "book" cost.

Income Adjustment Factor - an adjustment to the percent good factor that reflects an allowance for the reduction in income from a property as it becomes older.

Income Influence Method – a method of allocating the sale or stock and debt value of a business to different segments or subdivisions according to their contribution to the income of the business.

Income Tax Component - the part of the total capitalization rate that reflects the income taxes that a hypothetical purchaser would incur upon purchase of the subject property. This component is expressed as a relationship between the expected annual income tax expense and value.

J Factor - an adjustment made to straight-line depreciation in the calculation of the income tax component that reflects the relative benefits or disadvantages of the use of modified accelerated cost recovery system depreciation for determining income tax liabilities.

Land Reversion - the market value of land at the end of the remaining economic life of the assets (other than land) in a limited life CEA model. This value is discounted to the valuation date using the basic capitalization rate plus a component for ad valorem taxes.

Lessee - one who has the right to use or occupy property under a lease agreement; a tenant.

Lessor - one who owns the property under a lease agreement; a landlord.

Liabilities - claims held by non-owners on the assets of a business. Liabilities are obligations that a business is obliged to pay before the any claims of the owners are satisfied.

Lien date - All taxable property (both state and locally-assessed) is assessed annually for property tax purposes as of 12:01 a.m. on January 1, which is called the lien date. It is referred to as the lien date because on this date the taxes become a lien against all real property assessed on the secured roll.

Life Study – A survey or study of property lives by property category.

MACRS - the modified accelerated cost recovery system of depreciation allowed by the Internal Revenue Code.

Market Value – the amount of cash or its equivalent that property would bring if exposed for sale in the open market under conditions in which neither buyer nor seller could take advantage of the exigencies of the other and both with knowledge of all of the uses and purposes to which the property is adapted and for which it is capable of being used and of the enforceable restrictions upon those uses and purposes.

Net Book Value - the amount, in dollars, of an asset as carried in the accounting records of a business. The original cost of an asset less its accrued depreciation.

Noncapitalized Leased Property – leased property that is not reflected as a liability on a company's balance sheet.

Nonunitary Operations - income-producing activities engaged in by a public utility that are not essential to the provision of public utility services. Assets owned or used by a public utility that are not essential to provide public utility services are known as "Nonunitary Property".

Nonunitary Property - property not assessed as part of the unit.

Nonutility Operations - income-producing activities engaged in by the non-public utility segments of a business entity.

Normal Costs - costs typically expected in the construction or acquisition of a particular property type.

Percent Good - the complement of depreciation; if a property is 20 percent depreciated, its percent good is 80 percent. Percent good refers to the portion of benefits remaining in an asset compared to the total benefits when new.

R3 Survivor Curve – one of the asset retirement curves published by the Engineering Department at Iowa State University.

Rate Base - the dollar amount established by a regulatory agency upon which a return is allowed.

Rate of Return – see basic capitalization rate.

Recapture - the recovery by an investor of capital invested in a project or group of assets over a period of time. Also known as the return of the investment.

Replacement Cost - the cost to replace the subject property with a property that has equivalent utility as of the valuation date.

Reproduction Cost - the cost to reproduce an exact replica of the subject property as of the valuation date.

Reversion - a lump sum monetary benefit from a property that an investor receives or expects to receive at the termination of an investment.

Right of Way - an interest in real property that conveys the right to use a portion of another's property.

Single Life Method – in the individual or single life method, the percent good is simply a relationship between the present worth of an income for the probable remaining life expectancy and the present worth of an income for total life expectancy. The single life method assumes that the best estimate of the future life expectancy of survivors of a group of items is the average of the group.

Summation Method of Valuation – a valuation technique of combining values of individual assets or asset groups into one value.

Taxable Possessory Interest - a private right to the possession and use of publicly owned property for a period of time less than perpetuity.

Total Capitalization Rate – a capitalization rate that converts the income to be capitalized into a capitalized value. The rate includes the investors' perception of both return on and capital recapture of the investment, plus components for ad valorem property taxes and income taxes.

Trending Factor - an index number expressed in decimal form that estimates the change in cost over time. The trending factor is multiplied by the historical cost to calculate the reproduction or replacement cost new.

Unit Method of Valuation – The technique of valuing property operated as a unit in a primary function of the assessee as "one thing"

Unitary Operations – income-producing activities engaged in by a public utility that are essential to the prevision of public utility services. All property owned or used by a public utility that is needed to provide public utility services as known as "Unitary Property"

Working Cash – the amount of cash (or cash balance) required for payment of expenses that are due before the revenue is collected.

WSATA - Western States Association of Tax Administrators. WSATA is an association of tax administrators from twelve western states - Alaska, Arizona, California, Colorado, Idaho, Montana, Nevada, New Mexico, Oregon, Utah, Washington and Wyoming. Some of the goals of the association are to facilitate dialogue among tax administrators, industry representatives, and academicians; as well as to promote research on tax issues administered on the state level.

Yield Rate – see basic capitalization rate.